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The 1970 Pollution Exclusion in Comprehensive General Liability Policies: Reasons for Interpretations in Favor of Coverage in 1996 and Beyond

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The 1970 Pollution Exclusion in Comprehensive General Liability Policies: Reasons for Interpretations in Favor of Coverage in 1996 and Beyond

The events affecting the coverage claims before us span a period of several decades, in the course of which societal indifference concerning environmental pollution damage has been supplanted by a heightened awareness of the need for environmentally-sound waste-disposal practices and an increasingly aggressive governmental effort to remediate the consequences of past environmental damages. That evolution understandably has influenced the insurance industry's concern about its exposure for damages caused by environmental pollution, and has resulted in an industry-wide determination to modify the scope of insurance coverage for such damages.

The claims for coverage involve Comprehensive General Liability (CGL) policies covering plaintiff and its predecessors during the [1960's and 1970's,] issued by . . . a large number of . . . carriers. . . . [N]o dispute exists concerning the language of the critical provisions that affect the question of coverage. Because the policies are essentially standardized, industry-wide forms, our interpretation of their coverage provisions may affect significantly the allocation of damages for environmental pollution of . . . property among insurance carriers, industry and government.[1]

INTRODUCTION

Beginning with the introduction of Superfund in 1980,[2] the federal government and the states have cast a broad net of strict, joint and retroactive liability over business, industry and even individuals in an effort to marshall resources to pay for the daunting task of environmental remediation. Parties caught in this net have frequently turned to their third-party liability insurance carriers for coverage under Comprehensive General Lia-

1. Morton Int'l, Inc. v. General Accident Ins. Co., 629 A.2d 831, 833-34 (N.J. 1993) (Stein, J.), *cert. denied sub nom.* Insurance Co. of N. Am. v. Morton Int'l, 114 S. Ct. 2764 (1994).

2. Comprehensive Environmental Response, Compensation and Liability Act of 1980, Pub. L. No. 96-510, 94 Stat. 2767 (codified as amended at 42 U.S.C. §§ 9601-9675 (1988 & Supp. V 1993)).

bility ("CGL") policies. Because the collective cleanup liability is estimated to be in the hundreds of billions of dollars, insurers just as frequently dispute environmental claims. The defense most commonly raised by insurers in environmental coverage litigation is the "pollution exclusion," a clause which was almost universally included in CGL policies written from 1970 through 1986. Jurisdictions are split on the interpretation of the scope of the clause. However, reported decisions have become increasingly pro-insurer over the last few years. Many jurisdictions have yet to decide the issue, and billions of dollars in environmental coverage claims are potentially at stake, turning on the construction that courts may ascribe to a few critical words.

This comment, in response to the recent trend of pro-insurer decisions on the pollution exclusion, refines the classic pro-policyholder arguments using recent legal trends and insurance industry developments. It argues that a pro-coverage interpretation of the pollution exclusion is supported by modern contract law, equity and public policy.

Part I of this comment provides the history and background of environmental liabilities in the United States and describes the role of insurance. It also highlights the financial stakes of environmental coverage claims, reporting the most recent estimates of the ultimate environmental cleanup and transactions costs. Part II analyzes the various interpretive disputes surrounding the pollution exclusion and demonstrates the sharp split of authority. Part III describes the history of the development of the CGL policy and the pollution exclusion. Part IV reviews the classic theories supporting a pro-coverage interpretation of the pollution exclusion—contra insurer, estoppel and public policy—yet does so in light of modern movements in contract law as well as recent developments in the insurance industry.

I. ENVIRONMENTAL LIABILITIES AND INSURANCE COVERAGE

A. Environmental Cleanup Liability

In 1980, in the waning days of his administration, President Carter signed into law the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA" or "Superfund").[3] The law represented the federal response to na-

3. Pub. L. No. 96-510, 94 Stat. 2767 (codified as amended at 42 U.S.C. §§ 9601-9675. *See Remarks on Signing H.R. 7020 Into Law* (Dec. 11, 1980), *in* III PUB. PAPERS OF THE PRESIDENTS OF THE UNITED STATES—JIMMY CARTER 1980-1981 2797 (1982).

tional concerns raised by several high profile toxic contamination sites such as Love Canal, in Niagara Falls, New York and the "Valley of the Drums" in Shepardsville, Kentucky.[4] The ambitious goal of the law was to clean up hazardous sites throughout the United States which had been contaminated by historic waste disposal and toxic chemical management practices.[5] CERCLA established two primary mechanisms for implementation of the Superfund program: (1) a federal fund,[6] currently financed by a combination of taxes on petroleum,[7] chemical feedstocks[8] and corporate income,[9] appropriations from general revenues,[10] and certain costs and penalties recovered by the federal government;[11] and (2) a liability scheme under which the United States Environmental Protection Agency (the "EPA") can recover remediation costs from and order cleanups by Potentially Responsible Parties ("PRP's").[12] PRP's may include current site owners and operators, past site owners and operators, offsite generators of wastes, and waste transporters.[13]

The sweep of CERCLA's liability scheme is broad and was unprecedented at the time of the law's passage in 1980. CERCLA liability is strict[14]—PRP's may be liable for contamination caused by state of the art waste management practices which are in compliance with all applicable laws and regulations, and further may be held liable for conduct of their predecessors in interest[15] and third party waste contractors.[16] CERCLA liability is joint and several[17]—a PRP may be liable for the cleanup costs

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4. *See* H.R. REP. NO. 96-1016, Part I, 96th Cong., 2d Sess. 17-21, *reprinted in* 1980 U.S.C.C.A.N. 6119, 6119-23.

5. *Id.*

6. For the establishment of the Hazardous Substances Superfund and the enumerations of transfers to and expenditures from the fund, see 26 U.S.C. § 9507 (1994).

7. 26 U.S.C. § 4611 (1994).

8. *Id.* §§ 4661, 4671.

9. *Id.* § 59A.

10. 42 U.S.C. § 9611 (1988 & Supp. V 1993).

11. 26 U.S.C. § 9507(b)(2)-(5) (1994).

12. 42 U.S.C. § 9607 (1988).

13. *Id.* § 9607(a). CERCLA liability also depends on complex and well-litigated definitions of the terms "facility," "release" and "hazardous substances." *See id.* These subtleties of CERCLA liability are unimportant for the purposes of this comment. Therefore, this comment will use terms such as "site," "property," "contamination," "waste," "toxic chemicals," "pollution," etc. No technical or legal concepts are intended by such terms—they are to be understood in their common vernacular usage.

14. New York v. Shore Realty Corp., 759 F.2d 1032, 1042 (2d Cir. 1985).

15. *See, e.g.*, Kerr-McGee Chem. Corp. v. Lefton Iron & Metal Co., 14 F.3d 321, 325 (7th Cir. 1994).

16. *See, e.g.*, United States v. Shell Oil Co., 841 F. Supp. 962, 969-70 (C.D. Cal. 1993).

17. O'Neil v. Picillo, 883 F.2d 176, 178-79 (1st Cir. 1989), *cert. denied sub*

for an entire site, yet have only contributed a small amount of waste. CERCLA liability is retroactive[18]—PRP's can be held liable for conduct that occurred long before the dawn of Superfund.

Sites to be remediated under the Superfund program are placed on the National Priorities List (the "NPL"), which is intended to be a list of the very worst contaminated sites in the United States.[19] However, CERCLA is not the only law under which parties can incur liability for site cleanup.[20] Other federal remediation liability provisions include sections 3004(u), 3008(h) and 7003 of the Solid Waste Disposal Act[21] and section 311 of the Clean Water Act.[22] Additionally, after the enactment of CERCLA, many states established their own Superfund-like programs to address sites which the EPA did not list on the NPL.[23] As of 1993, forty-three states had established such programs.[24]

B. The Role of Insurance

Parties which have incurred cleanup liability under these broad statutes have sought to offset some of their losses by turning to their insurance carriers for coverage. Such claims are often made under Comprehensive General Liability ("CGL") policies,[25]

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nom. American Cyanamid Co. v. O'Neil, 493 U.S. 1071 (1990).

18. United States v. Northeastern Pharmaceutical & Chem. Co., 810 F.2d 726, 732-34 (8th Cir. 1986), *cert. denied*, 484 U.S. 848 (1987).

19. *See* 42 U.S.C. § 9605(a)(8) (1988); 40 C.F.R. § 300.4 (1995) (defining NPL). For the current NPL, see 40 C.F.R. § 300 app. B (1995). For the EPA's Hazard Ranking System, which is the method whereby the EPA makes NPL listing decisions, see *id.* § 300 app. A. Through 1995, the EPA had identified over 40,000 sites in the United States as potential candidates for inclusion on the NPL. INSURANCE SERVICES OFFICE, INC., SUPERFUND AND THE INSURANCE ISSUES SURROUNDING ABANDONED HAZARDOUS WASTE SITES 8-10 & fig. 2 (1995) (citations omitted) [hereinafter ISO REPORT]. As of November, 1995, the EPA had listed a total of 1,374 such sites since 1980, 84 of which have been deleted, leaving a net of 1,290 sites. *Id.* at 14 tbl. 4 (citations omitted).

20. This comment refers to sites on the NPL as NPL sites, and refers to sites for which cleanup liability is imposed under other federal or state programs as non-NPL sites.

21. 42 U.S.C. §§ 6924(u), 6928(h), 6973 (1988) (respectively). This statute is also known as the Resource Conservation and Recovery Act.

22. 33 U.S.C. § 1321 (1994).

23. RIDGWAY M. HALL, JR. ET AL., SUPERFUND MANUAL—LEGAL AND MANAGEMENT STRATEGIES § 11.2, at 11-7 (1993).

24. HALL, *supra* note 23, § 11.2, at 11-7. For a table of the state Superfund-like statutes, their statutory authority and lead agency contacts, see *id.* § 11.2, at 11-28 to 11-43.

25. *See* GRACE A. CARTER & KEITH A. MEYER, ENVIRONMENTAL INSURANCE HANDBOOK § 3.2.1, at 30 (1992). CGL policies provide the policyholder with broad coverage for a variety of liabilities that it may incur to third parties. *Id.* In 1986, the title of the standard CGL policy was changed to "*Commercial* General Liability."

which are frequently purchased by business enterprises.[26] The standard CGL policy provides that "[the insurer] will pay on behalf of the insured all sums which the insured shall become legally obligated to pay as *damages* because of . . . bodily injury or . . . property damage to which this [policy] applies, *caused by an occurrence*."[27] This is referred to as an *occurrence-based* policy because the insured is covered if the *occurrence* happens within the policy period, even if the claim arises after the policy period.[28] This is contrasted with a *claims-made* policy which covers the insured if the insured makes a *claim* for damages within the policy period.[29]

An *occurrence* is defined in the standard CGL policy as "an accident, including continuous or repeated exposure to conditions, which results in bodily injury or property damage neither expected nor intended from the standpoint of the insured."[30] In 1970, a new exclusion was added to the standard CGL policy which is commonly referred to as the "pollution exclusion."[31] The pollution exclusion reads:

> This insurance does not apply . . .
>
> . . . .
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> (f) to bodily injury or property damage arising out of the discharge, dispersal, release or escape of smoke, vapors, soot, fumes, acids, alkalis, toxic chemicals, liquids or gasses, waste materials or other irritants, contaminants or pollutants into or upon land, the atmosphere or any water course or body of water; but this exclusion does not apply if such discharge, dispersal, release or escape is sudden and accidental.[32]

EDWARD J. ZULKEY, BUSINESS LIABILITY INSURANCE—LITIGATION, ARBITRATION AND SETTLEMENT § 1.08, at 1-18 n.113. Both the pre-1986 and the post-1986 policies are generally referred to as CGL policies, and are accordingly so referenced throughout this comment.

See infra Part III for a history of the development of the standard CGL policy.

26. ROWLAND H. LONG, 2 THE LAW OF LIABILITY INSURANCE § 11A.01, at 11A-3 (1992) (citations omitted).

27. 1973 Comprehensive General Liability Insurance Policy, *reprinted in* TOD I. ZUCKERMAN & MARK C. RASKOFF, ENVIRONMENTAL INSURANCE LITIGATION PRACTICE FORMS Form VI-2, at VI-23 (1995) (emphasis added) [hereinafter 1973 CGL Policy].

28. CARTER & MEYER, *supra* note 25, § 3.2.2, at 32.

29. *Id.* § 3.2.2, at 33. In 1986, the insurance industry introduced a standard claims-made CGL policy. *Id.* § 3.2.2, at 32-33. However, for the purpose of this comment, the only relevant CGL policies are those issued prior to 1986.

30. 1973 CGL Policy, *supra* note 27, at VI-20.

31. Robert S. Soderstrom, *The Role of Insurance in Environmental Litigation*, 11 FORUM 762, 766 & n.19 (1976). In 1970, the clause was introduced as a mandatory endorsement, and in 1973 was incorporated into the policy itself as exclusionary clause "f." *Id.* at 766-68.

32. 1973 CGL Policy, *supra* note 27, at VI-23. This clause is also commonly referred to as the "qualified pollution exclusion," the "conditional pollution exclusion," or the "sudden and accidental pollution exclusion" in order to differentiate it from

The pollution exclusion was universally included in CGL policies issued to insureds from 1970 until 1986, at which time it was replaced by the "absolute pollution exclusion."[33] The absolute pollution exclusion does not include an exception for "sudden and accidental" discharges, and has been almost uniformly held to be an absolute bar to coverage for environmental claims.[34] However, because the standard CGL policy is an occurrence-based policy, the pollution exclusion contained in CGL policies written from 1970 through 1986 still has great relevance to

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the "absolute pollution exclusion." Throughout this comment, this clause is referred to simply as the "pollution exclusion." When referencing the absolute pollution exclusion, this comment will uses the term "absolute pollution exclusion."

33. Michelle I. Schaffer, *The Evolution of the Pollution Exclusion: From "Sudden and Accidental" to Absolute and Unambiguous*, *in* REFERENCE HANDBOOK ON THE COMPREHENSIVE GENERAL LIABILITY POLICY: COVERAGE PROVISIONS, EXCLUSIONS, AND OTHER LITIGATION ISSUES 209, 225 (1995). The absolute pollution exclusion reads:

> This insurance does not apply to:
>
> f.(1) "Bodily injury" or "property damage" arising out of the actual, alleged or threatened discharge, dispersal, release or escape of pollutants:
>
> (a) At or from premises you own, rent or occupy;
>
> (b) At or from any site or location used by or for you or others for the handling, storage, disposal, processing or treatment of waste;
>
> (c) Which are at any time transported, handled, stored, treated, disposed of, or processed as waste by or for you or any person or organization for whom you may be legally responsible; or
>
> (d) At or from any site or location on which you or any contractors or subcontractors working directly or indirectly on your behalf are performing operations:
>
> (i) if the pollutants are brought on or to the site or location in connection with such operations; or
>
> (ii) if the operations are to test for, monitor, clean up, remove, contain, treat, detoxify or neutralize pollutants.
>
> . . . .
>
> Pollutants means any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste. Waste includes materials to be recycled, reconditioned or reclaimed.

Id. at 225-26.

34. *See* National Union Fire Ins. Co. v. CBI Indus., Inc., 907 S.W.2d 517, 522 & n.8 (Tex. 1995) ("This pollution exclusion is just what it purports to be—absolute.") (quoting Alcolac Inc. v. California Union Ins. Co., 716 F. Supp. 1546, 1549 (D. Md. 1989)). *See also* Schaffer, *supra* note 33, at 228-32. *See* Steven A. Miller & Julianne L. Swilley, *The Absolute Pollution Exclusion in General Liability Insurance Policies*, *in* REFERENCE HANDBOOK ON THE COMPREHENSIVE GENERAL LIABILITY POLICY: COVERAGE PROVISIONS, EXCLUSIONS, AND OTHER LITIGATION ISSUES 145 (1995).

The primary interpretive issue currently developing in the courts regarding the absolute pollution exclusion focuses on its applicability to personal injury from exposure to toxic substances in situations outside the classical setting of contamination of environmental media. *See, e.g.*, Stoney Run Co. v. Prudential-LMI Commercial Ins. Co., 47 F.3d 34 (2d Cir. 1995) (carbon monoxide poisoning in the home); Essex Ins. Co. v. Avondale Mills, Inc., 639 So. 2d 1339 (Ala. 1994) (occupational asbestos exposure); Sullins v. Allstate Ins. Co., 667 A.2d 617 (Md. 1995) (childhood lead poisoning from ingestion of paint chips in the home).

today's coverage claims for environmental damages arising out of occurrences which happened in that decade and a half.

C. *Resources, Transaction Costs and Claim Disputes*

The stakes in the environmental cost allocation game between policyholders and their insurers could not be higher. In the early 1990's, estimates of the total cost of cleanup for all contaminated sites in the United States (NPL and non-NPL) were estimated in the range of 150 billion to one trillion dollars.[35] Current best estimates are a bit lower, at anywhere from 80 to 167 billion dollars for NPL sites[36] and 75 billion dollars for non-NPL sites.[37]

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35. *See* Thomas M. Reiter et al., *The Pollution Exclusion Under Ohio Law: Staying the Course*, 59 CINCINNATI L. REV. 1165, 1171 & n.30 (1991).

36. A.M. BEST CO., P/C INDUSTRY BEGINS TO FACE ENVIRONMENTAL AND ASBESTOS LIABILITIES 8 exhibit 6 (1996) (collecting mid-range estimates of five recent studies) [hereinafter BEST REPORT]. The A.M. Best Company analyzes the insurance industry and publishes ratings and other financial information. *Id.* at 26.

37. BEST REPORT, *supra* note 36, at 10. It is this author's opinion that the recent political movement toward smaller, more cost-effective government and an increasing consensus that Superfund is not fair, does not work and costs too much is the ultimate factor influencing the reductions in the cost estimates. For a critique of the Superfund liability system and its resultant inefficiencies and inequities, see generally Jerry L. Anderson, *The Hazardous Waste Land*, 13 VA. ENVTL. L.J. 1 (1993). For a critique of the Superfund cleanup remedy selection process, see generally Robert H. Abrams, *Using Experience to Improve Superfund Remedy Selection*, 29 U. RICH. L. REV. 581 (1995).

As evidence of the trend toward a less costly national environmental cleanup program, note that the addition of new sites to the NPL by the EPA has slowed appreciably in recent years—in the six years between 1983 and 1989, the number of sites on the NPL grew from zero to 1,224, but in the following six year period, the number of NPL sites increased only from 1,224 to 1,290. ISO REPORT, *supra* note 19, at 10 fig. 3 (citations omitted). The A.M. Best Company has recently estimated the ultimate number of NPL sites at 2,100—down from its 1994 estimate of 4,600. BEST REPORT, *supra* note 36, at 8 exhibit 6.

Superfund reform initiatives have been introduced in both the 103d and 104th Congresses. *See* Superfund Reform Act of 1994, H.R. 3800, 103d Cong., 2d Sess. (1994); Reform of Superfund Act of 1995, H.R. 2500, 104th Cong., 1st Sess. (1995). These bills include reforms in the liability scheme as well as provisions for more cost-effective remedy selections. *See also* H.R. 3800 §§ 401-413, 501-506; H.R. 2500 §§ 201-216, 102 (respectively). Although no bill has passed as of the writing of this comment, the consensus of Congress—and what it perceives to be the consensus of its constituents—is toward a more cost-effective environmental cleanup program.

State lawmakers are also responding to this consensus with what is commonly referred to as "Brownfields" programs which are designed to encourage cleanup and reuse of industrial sites through less onerous liability provisions and cleanup standards. *See* James W. Creenan & John Q. Lewis, *Pennsylvania's Land Recycling Program: Solving the Brownfields Problem with Remediation Standards and Limited Liability*, 34 DUQ. L. REV. 661, 673-74 & n.71 (1996).

It is perhaps these trends which have influenced the A.M. Best Company to reduce its 1996 estimate of total NPL cleanup costs to 54-108 billion dollars, down from its 1994 estimate of 120-600 billion dollars. BEST REPORT, *supra* note 36, at 8 exhibit 6.

The United States insurance industry's share of this tab is currently estimated at between forty-eight and ninety-one billion dollars, with a best estimate of sixty-six billion dollars.[38]

Not only is the size of the cleanup bill daunting, but unfortunately much of it is spent on excessive transaction costs associated with assigning environmental liability. Transaction costs are the monies spent by various stakeholders—governments, PRP's, insurers and the community—contesting and allocating liability amongst themselves.[39] The Rand Institute for Civil Justice has estimated that transaction costs constitute thirty-two percent of all money spent by private sector PRP's through 1991 in managing Superfund liabilities.[40] For insurers, however, the transaction costs dwarf the monies spent on actual cleanup—transaction costs were eighty-eight percent of all insurers' Superfund-related expenditures through 1991, almost half of which was devoted to disputing claims with policyholders.[41] For insurers, this level of transaction costs is more than twice as high as that experienced for non-environmental CGL claims where insurers generally do not dispute coverage and thereby make more indemnity payments.[42]

Insurers have found it to be in their best interests to dispute environmental claims[43] and therefore "[i]nsurers and insureds are engaged in 'a fight for their financial lives,'"[44] played out on the battlefield of environmental coverage litigation.

II. ENVIRONMENTAL COVERAGE LITIGATION AND INTERPRETATION OF THE POLLUTION EXCLUSION

In disputing coverage for environmental claims, the three defenses most commonly raised by insurers are: (1) remediation costs incurred at the insistence of governmental regulators are not "damages,"[45] (2) the damages do not fall within the defini-

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38. BEST REPORT, *supra* note 36, at 6 exhibit 3.

39. *See* LLOYD S. DIXON, FIXING SUPERFUND—THE EFFECT OF THE PROPOSED SUPERFUND REFORM ACT OF 1994 ON TRANSACTION COSTS xvi-xvii (1994) [hereinafter FIXING SUPERFUND].

40. FIXING SUPERFUND, *supra* note 39, at 5.

41. *Id.* at 41-43 & fig. 4.1.

42. JAN PAUL ACTON & LLOYD S. DIXON, SUPERFUND AND TRANSACTION COSTS—THE EXPERIENCE OF INSURERS AND VERY LARGE INDUSTRIAL FIRMS 30 (1992).

43. *See* LLOYD S. DIXON ET AL., PRIVATE-SECTOR CLEANUP EXPENDITURES AND TRANSACTION COSTS AT 18 SUPERFUND SITES 56 (1993) ("Many firms spend money on coverage disputes with their insurers, but few receive reimbursement. . . . Overall, insurers reimbursed PRP's for approximately 8 percent of their expenditures.") [hereinafter 18 SUPERFUND SITES].

44. Reiter et al., *supra* note 35, at 1172 (citations omitted).

45. *See, e.g.*, Aetna Casualty & Sur. Co. v. General Dynamics Corp., 968 F.2d

tion of "occurrence" because they were expected or intended by the insured,[46] and (3) the pollution exclusion operates as a bar to coverage. Of these three defenses, the one most increasingly relied upon by insurers is the pollution exclusion.[47]

Insurance contracts are generally governed by state law, and jurisdictions are split on the interpretation of the pollution exclusion.[48] Therefore, "disagreement between insureds and insurers concerning the meaning of [the pollution exclusion] has precipitated 'a legal war . . . in state and federal courts from Maine to California.'"[49] The majority of the battles in the pollution exclusion war involve the exception to the exclusion—"but this exclusion does not apply if such discharge, dispersal, release, or escape is sudden and accidental," and in particular the phrase "sudden and accidental."[50] The primary interpretive disputes surrounding this exception are outlined below.[51]

707, 712-13 (8th Cir. 1992); New Castle County v. Hartford Accident & Indem. Co., 933 F.2d 1162, 1184-90 (3d Cir. 1991); Hazen Paper Co. v. United States Fidelity & Guar. Co., 555 N.E.2d 576, 582-84 (Mass. 1990); Morton Int'l, Inc. v. General Accident Ins. Co., 629 A.2d 831, 843-47 (N.J. 1993), *cert. denied*, 114 S. Ct. 2764 (1994). In such disputes, insurers typically argue that "damages" connotes a legal remedy, while an administrative order to clean up a site is an equitable action. *See New Castle County*, 933 F.2d at 1185.

46. *See, e.g.*, Broderick Inv. Co. v. Hartford Accident & Indem. Co., 954 F.2d 601, 605-06 (10th Cir.), *cert. denied*, 506 U.S. 865 (1992); *New Castle County*, 933 F.2d at 1191-92; *Morton*, 629 A.2d at 877-84. *See supra* note 30 and accompanying text for the definition of "occurrence" in the standard CGL policy.

47. *Increasing Reliance on Pollution Exclusion*, ENVT'L LIAB. REP., Jan. 1, 1995, at 14 (Often, "little else stands between [insurers] and [indemnifying their policyholders] in most of these cases.").

48. *See* FIXING SUPERFUND, *supra* note 39, at 41.

Consequently, in a dispute between an insurer and a policyholder where the insurer has raised the pollution exclusion as a bar to coverage, the question of choice-of-law is exceedingly important and may be determinative. *See, e.g.*, General Ceramics Inc. v. Firemen's Fund Ins. Co., 66 F.3d 647 (3d Cir. 1995) (choosing between the applicability of Pennsylvania's pro-insurer interpretation and New Jersey's pro-policyholder interpretation); American Motorists Ins. Co. v. ARTRA Group, Inc., 659 A.2d 1295 (Md. 1995) (choosing between the applicability of Maryland's pro-insurer interpretation and Illinois's pro-policyholder interpretation).

49. Northern Ins. Co. of N.Y. v. Aardvark Assoc., Inc., 942 F.2d 189, 191 (3d Cir. 1991) (citations omitted).

50. *See* Stanley M. Spracker et al., *A Trial Lawyer's Perspective on the Pollution Exclusion*, 25 ENV'T L. REP. 10065, 10068 (1995) ("Seldom in the history of contract law have three words generated so much controversy.").

51. In addition to disputes as to the interpretation of the exception, there is also the question of upon whom the burden of proof rests to prove the applicability of the exclusion—the insurer or the policyholder. Courts generally agree that the burden of establishing a prima facie case of coverage—proving that there is an "occurrence" in an occurrence-based policy—is on the policyholder, and that the burden shifts to the insurer to prove the applicability of any policy exception as an affirmative defense. *See, e.g.*, SCSC Corp. v. Allied Mut. Ins. Co., 536 N.W.2d 305, 313 (Minn. 1995). However, courts are split as to the placement of the burden of proving

A. What Does "Sudden" Mean?

Environmental contamination commonly occurs through gradual migration of contaminants through soil, groundwater, surface water or sediments, often over a period of years or even decades. Common scenarios include a landfill leaching pollutants, an underground storage tank leaking petroleum, or an industrial facility which has become contaminated through multiple spills and leaks from routine operations.

If the term "sudden" is interpreted as having a temporal element, i.e., meaning abrupt or instantaneous, then environmental damages arising out of the common scenarios described above would not fall into the exception to the pollution exclusion and therefore coverage under the standard CGL policy would be precluded. Alternatively, if "sudden" is interpreted without a temporal component—simply meaning "unexpected and unintended"—then coverage is not automatically precluded for gradual polluting events.

1. Plain Meaning, Ambiguity and Dictionary Definitions

Insurers argue that one of the canons of insurance contract construction is the plain meaning rule—that if unambiguous on their face, words are to be given their plain, everyday and popular meaning—and that the plain meaning of "sudden" includes a temporal element.[52]

Policyholders, however, point to conflicting dictionary definitions of the word "sudden" as evidence that there is more than one reasonable interpretation of the clause, and it is therefore ambiguous, so the plain meaning rule does not apply.[53] The defi-

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the applicability of the exception to the pollution exclusion, most holding that once the insurer has established that the exclusion applies, the burden of proving restoration of coverage under the exception is on the policyholder. *See, e.g.*, Employers Ins. of Wausau v. Petroleum Specialties, Inc., 69 F.3d 98, 102 (6th Cir. 1995); Harrow Prods., Inc. v. Liberty Mut. Ins. Co., 64 F.3d 1015, 1020 (6th Cir. 1995); *SCSC Corp.*, 536 N.W.2d at 314. *But see* Edo Corp. v. Newark Ins. Co., 878 F. Supp. 366, 371 (D. Conn. 1995).

52. *See* Hybud Equip. Corp. v. Sphere Drake Ins. Co., 597 N.E.2d 1096, 1101 (Ohio 1992), *cert. denied*, 507 U.S. 987 (1993). *See also* Michael W. Peters, Note, *Insurance Coverage for Superfund Liability: A Plain Meaning Approach to the Pollution Exclusion Clause*, 27 WASHBURN L.J. 161 (1987); GEORGE J. COUCH, 2 COUCH ON INSURANCE 2d § 15:18, at 191 (1984) ("Indeed, if there is no ambiguity in the insurance contract it is the duty of the court to apply to the words used their ordinary meaning and not favor either party in the construction."). For further discussion of the plain meaning rule, see *infra* Part IV.A.1.

53. *See* Claussen v. Aetna Casualty & Sur. Co., 380 S.E.2d 686, 688 (Ga.

nitions of "sudden" in some standard dictionaries include a temporal component such as "abruptness;" while others focus exclusively on unexpectedness.[54] Therefore, argue policyholders, because ambiguities in an insurance contract are to be construed against the insurer, the interpretation in favor of coverage should be adopted.[55]

2. *Giving Effect to All Terms*

Insurers also point to another uniformly recognized canon of insurance policy construction—that all terms be given meaning and effect.[56] They note that "accidental" already connotes unexpectedness, and conclude that a definition of "sudden" without a temporal component would render "accidental" redundant and therefore superfluous.[57]

In response to the anti-redundancy argument, policyholders

1989).

54. *Claussen*, 380 S.E.2d at 688.

The primary definition of "sudden" in Webster's is "happening without previous notice or with very brief notice: coming or occurring unexpectedly: not foreseen or prepared for." WEBSTER'S THIRD INT'L DICTIONARY 2284 (1986). The tertiary definition of "sudden" in Webster's is "made, provided, brought about, or acting in a short time: prompt, immediate . . . on the spur of the moment." *Id.*

The primary definition of "sudden" in Oxford's is "[o]f actions, events conditions: Happening or coming without warning or premonition; taking place or appearing all at once." 10 THE OXFORD ENGLISH DICTIONARY Su-Sz 96 (1933). The tertiary definition of sudden in Oxford's is "[p]erformed or taking place without delay; speedy; prompt, immediate." *Id.* at 97.

Black's Law Dictionary defines "sudden" as "[h]appening without previous notice or with very brief notice; coming or occurring unexpectedly; unforseen; unprepared for." BLACK'S LAW DICTIONARY 1432 (6th ed. 1990).

55. *See infra* Part IV.A. for a discussion of the rule of contra insurer. *See also* John S. Vishneski III et al., *The Insurance Industry's 1970 Pollution Exclusion: An Exercise in Ambiguity*, 23 LOY. U. L.J. 67 (1991).

56. *See* COUCH, *supra* note 52, § 15:44, at 268-73 ("When reasonably possible, . . . operation, effect, and meaning should be given to each and every sentence, clause, and word of a contract of insurance.").

57. *See, e.g.*, Charter Oil Co. v. American Employers' Ins. Co., 69 F.3d 1160, 1164-65 (D.C. Cir. 1995); United States Fidelity & Guar. Co. v. Morrison Grain Co., 999 F.2d 489, 493 (10th Cir. 1993); Aetna Casualty & Sur. Co. v. General Dynamics Corp., 968 F.2d 707, 710 (8th Cir. 1992); A. Johnson & Co. v. Aetna Casualty & Sur. Co., 933 F.2d 66, 73 (1st Cir. 1991); Dimmitt Chevrolet, Inc. v. Southeastern Fidelity Ins. Corp., 636 So. 2d 700, 704 (Fla. 1993) (citations omitted); Hybud Equip. Corp. v. Sphere Drake Ins. Co., 597 N.E.2d 1096, 1101 (Ohio 1992), *cert. denied*, 507 U.S. 987 (1993).

However, the Third Circuit Court of Appeals proffered that, without a temporal component, "sudden" would *not* be synonymous with "accidental" because accidental means "unintended" and sudden means "unexpected." New Castle County v. Hartford Accident & Indem. Co., 933 F.2d 1162, 1194 (3d Cir. 1991) ("To the extent that the meanings of these words overlap, we do not think that this preclude[s a court] from defining sudden as unexpected.").

point out that redundancies are common in insurance policy legalese and point to strings of terms in the pollution exclusion itself such as "smoke, vapors, soot, fumes, acids, alkalis, toxic chemicals, liquids or gases" and "discharge, dispersal, release or escape."[58] However, insurers respond that the anti-redundancy cannon has more importance when the terms are used in the conjunctive, (with the conjunction "and" as in the phrase "sudden and accidental") than when the terms are used in the disjunctive (with the conjunction "or").[59] Furthermore, insurers argue that terms such as "discharge, dispersal, release, or escape" have different shades of meaning, each of which may add a critical element of application to the phrase.[60]

There is also a pro-coverage argument which relies on the canon of giving effect to all terms: reconciling "sudden and accidental" with the definition of "occurrence." The standard CGL policy defines "occurrence" as "an accident, including continuous or repeated exposure to conditions, which results in bodily injury or property damage neither expected or intended from the standpoint of the insured."[61] Therefore, "accident" includes "continuous or repeated exposure to conditions." If "sudden" were interpreted to mean "instantaneous," insureds argue, then the phrase "sudden and accidental" would be inherently contradictory—instantaneous *and* continuous or repeated.[62]

3. Previous Judical Construction

Policyholders also argue that, prior to the introduction of the pollution exclusion, the phrase "sudden and accidental" had been used for many years in boiler and machinery policies, and had been interpreted by courts to simply mean "unexpected and unintended," with no temporal element.[63] Another of the canons of insurance policy interpretation holds that "[t]he judical construction placed upon particular words or phrases made prior to the issuance of a policy employing them will be presumed to have

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58. *See Charter Oil*, 69 F.3d at 1164; Outboard Marine Corp. v. Liberty Mut. Ins. Co., 607 N.E.2d 1204, 1220 (Ill. 1992).

59. *Charter Oil*, 69 F.3d at 1164.

60. *Id.*

61. 1973 CGL Policy, *supra* note 27, at VI-20.

62. *See* Hecla Mining Co. v. New Hampshire Ins. Co., 811 P.2d 1083, 1092 (Colo. 1991); *Outboard Marine*, 607 N.E.2d at 1219.

63. *See* Morton Int'l, Inc. v. General Accident Ins. Co., 629 A.2d 831, 863-65 (N.J. 1993) (citing New England Gas & Elec. Ass'n v. Ocean Accident & Guarantee Corp., 116 N.E.2d 671 (Mass. 1953), *cert. denied*, 114 S. Ct. 2764 (1994). *See also* New Castle County v. Hartford Accident & Indem. Co., 933 F.2d 1162, 1197 (3d Cir. 1991)).

been the construction intended to be adopted by the parties."[64] Therefore, policyholders argue, the phrase "sudden and accidental" in the pollution exclusion clause should be afforded the same pre-1970 construction applied by courts when interpreting boiler and machinery policies.[65]

The case most commonly cited for the proposition that "sudden and accidental" was judicially construed in boiler and machinery policies prior to 1970 to mean "unexpected and unintended" and to include damages that develop gradually is *New England Gas & Electric Ass'n v. Ocean Accident & Guaranty Corp.*[66] In *New England Gas*, the insured owned a turbine generator that was covered by a boiler and machinery policy which covered loss resulting from an accident.[67] The policy defined "accident" as "a sudden and accidental breaking, deforming, burning out or rupturing" of the machinery.[68] The insured lost the use of a turbine due to a crack in the spindle which, during an inspection after the unit was taken out of service, was found to have formed over a period of 2.4 to 10 hours.[69] The court found for the insured, rejecting the notion that "sudden," as used in the policy, connoted "any idea of rapidity or quickness."[70] The court stated:

> [We] give to the term sudden its primary meaning according to lexicographers as happening without previous notice or with very brief notice, or as something coming or occurring unexpectedly, unforseen, or unprepared for . . . . The damage to the spindle could not be reasonably antici-

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64. *Morton*, 629 A.2d at 863 (quoting COUCH, *supra* note 52, § 15:20, at 195-96).

65. *See* Carl A. Salisbury, *Pollution Liability Insurance Coverage, The Standard-Form Pollution Exclusion, and the Insurance Industry: A Case Study in Collective Amnesia*, 21 ENVTL. L. 357, 379-82. (1991).

66. 116 N.E.2d 671, 680-81 (Mass. 1953). *See also* Julius Hyman & Co. v. American Motorists Ins. Co., 136 F. Supp. 830, 832-33 (D. Colo. 1955); City of Detroit Lakes v. Travelers Indem. Co., 275 N.W. 371, 372 (Minn. 1937); Anderson & Middleton Lumber Co. v. Lumbermen's Mut. Casualty Co., 333 P.2d 938, 940-41 (Wash. 1959). *But see* Cornell Wood Prods. Co. v. Hartford Steam Boiler Inspection & Ins. Co., 62 F. Supp. 303, 305 (N.D. Ill. 1945).

After 1970, courts continued to interpret "sudden and accidental" in boiler and machinery policies to include equipment failures that develop gradually. *See* Community Fed. Sav. & Loan Ass'n v. Hartford Steam Boiler Inspection & Ins. Co., 580 F. Supp. 1170, 1173 (E.D. Mo. 1984); Cyclops Corp. v. Home Ins. Co., 352 F. Supp. 931, 934 (W.D. Pa. 1973).

See also GEORGE J. COUCH, 10A COUCH ON INSURANCE 2d § 42:396, at 505 (1982) ("When coverage is limited to a sudden 'breaking' of machinery the word 'sudden' should be given its primary meaning as happening without previous notice, or as something coming or occurring unexpectedly, as unforseen and unprepared for. That is, 'sudden' is not to be construed as synonymous with instantaneous.").

67. *New England Gas*, 116 N.E.2d at 675.

68. *Id.*

69. *Id.* at 678.

70. *Id.* at 680.

pated, and its occurrence was unexpected and unforseen and consequently sudden in the ordinary meaning of the word.[71]

Similarly, in *Anderson & Middleton Lumber Co. v. Lumbermen's Mutual Casualty Co.*,[72] a band saw covered by a boiler and machinery policy was shut down due to a broken wheel that, according to expert testimony, had gradually developed a crack over a period of one day to three weeks.[73] The court reviewed conflicting dictionary definitions—one affording "sudden" a temporal component and one focusing only on the "unexpectedness" of "sudden."[74] The court noted that the purpose of the policy language was to afford the insured protection for equipment breakdown which was unavoidable—but to preclude coverage if the insured behaved recklessly.[75] However, the court concluded, this purpose would not be promoted by interpreting "sudden" as "instantaneous," thereby precluding coverage for undetectable defects which developed gradually and could not have been avoided by the insured.[76] In finding for the insured, the court proffered that the purpose of the policy would be promoted by interpreting sudden as "unforseen and unexpected."[77]

4. Split of Judicial Authority

The highest courts of fifteen states have had the occasion to decide if "sudden," in the pollution exclusion clause, carries a temporal element, and the courts are almost evenly split. The

71. *Id.* at 680-81.
72. 333 P.2d 938 (Wash. 1959).
73. *Anderson & Middleton Lumber*, 333 P.2d at 940.
74. *Id.*
75. *Id.* at 940-41.
76. *Id.*
77. *Id.*

highest courts of Oklahoma,[78] Minnesota,[79] Maryland,[80] Massachusetts,[81] Michigan,[82] Florida,[83] Ohio,[84] and North Carolina[85] have afforded "sudden" a temporal element. The highest courts of Washington,[86] South Carolina,[87] Illinois,[88] West Virginia,[89] Colorado,[90] Wisconsin,[91] and Georgia[92] have held that "sudden" has no temporal element and simply means

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78. *See* Kerr-McGee Corp. v. Admiral Ins. Co., 905 P.2d 760, 763-64 (Okla. 1995).

79. *See* Board of Regents v. Royal Ins. Co. of Am., 517 N.W.2d 888, 892 (Minn. 1994).

80. *See* American Motorists Ins. Co. v. ARTRA Group, Inc., 659 A.2d 1295, 1308 (Md. 1995).

81. *See* Lumbermens Mut. Casualty Co. v. Belleville Indus., Inc., 555 N.E.2d 568, 572 (Mass. 1990).

82. *See* Upjohn Co. v. New Hampshire Ins. Co., 476 N.W.2d 392, 394 (Mich. 1991).

83. *See* Dimmitt Chevrolet, Inc. v. Southeastern Fidelity Ins. Corp., 636 So. 2d 700, 704 (Fla. 1993) (four-to-three decision with vigorous dissent). *Dimmitt* involved an insured that sold used crankcase oil to a recycler and subsequently became liable under CERCLA for the cleanup of petroleum contamination at the recycler's facility. *Dimmitt*, 636 So. 2d at 701. Demonstrative of the sharp split of opinion on this issue is the fact the Supreme Court of Florida, also in a four-to-three decision, had only ten months earlier filed an opinion in *Dimmitt* in which the court reached the opposite result. *See* Dimmitt Chevrolet, Inc. v. Southeastern Fidelity Ins. Co., 35 Env't Rep. Cas. (BNA) 1700 (Fla. 1992), *withdrawn and substituted by* 636 So. 2d 700 (Fla. 1993). The swing vote was Justice Grimes, who, in a concurring opinion that reads more like a coerced confession, states:

> I originally concurred with the position of the dissenters in this case. I have now become convinced that I relied too much on what was said to be the drafting history of the pollution exclusion clause and perhaps subconsciously upon the social premise that I would rather have insurance companies cover these losses rather than parties such as Dimmitt who did not actually cause the pollution damage. In doing so, I departed from the basic rule of interpretation that language should be given its plain and ordinary meaning. Try as I will, I cannot wrench the words "sudden and accidental" to mean "gradual and accidental," which must be done in order to provide coverage in this case.

Dimmitt, 636 So. 2d at 706 (Grimes, J., concurring).

84. *See* Hybud Equip. Corp. v. Sphere Drake Ins. Co., 597 N.E.2d 1096, 1102 (Ohio 1992), *cert. denied*, 507 U.S. 987 (1993).

85. *See* Waste Management of Carolinas, Inc. v. Peerless Ins. Co., 340 S.E.2d 374, 382 (N.C. 1986).

86. *See* Queen City Farms, Inc. v. Central Nat'l Ins. Co. of Omaha, 882 P.2d 703, 720-25 (Wash. 1994).

87. *See* Greenville County v. Insurance Reserve Fund, 443 S.E.2d 552, 553 (S.C. 1994).

88. *See* Outboard Marine Corp. v. Liberty Mut. Ins. Co., 607 N.E.2d 1204, 1220 (Ill. 1992).

89. *See* Joy Technologies, Inc. v. Liberty Mut. Ins. Co., 421 S.E.2d 493, 500 (W. Va. 1992).

90. *See* Hecla Mining Co. v. New Hampshire Ins. Co., 811 P.2d 1083, 1092 (Colo. 1991).

91. *See* Just v. Land Reclamation, Ltd., 456 N.W.2d 570, 573 (Wis. 1990).

92. *See* Claussen v. Aetna Casualty & Sur. Co., 380 S.E.2d 686, 688 (Ga. 1989).

"unexpected and unintended." Most federal courts of appeal sitting in diversity have found "sudden" to have a temporal element.[93]

B. What is the Relationship Between the Pollution Exclusion and the Definition of "Occurrence?"

Courts have also addressed the relationship between the occurrence definition and the pollution exclusion. This is a particularly relevant question for courts which conclude that "sudden" has no temporal component, and therefore that "sudden and accidental" means "unexpected and unintended"—the operative language in the occurrence definition.[94] In the pollution exclusion, is it the discharge which must be unexpected and unintended, or the resultant environmental damage? If it is the damage, as in the occurrence definition, then the pollution exclusion and the occurrence definition are simply co-extensive—any damage, pollution-related or otherwise, which is expected or intended is already excluded from coverage by the standard CGL policy occurrence definition.

Most courts which have considered the question have concluded that the focus of the exception—"but this exclusion does not apply if *such discharge, dispersal, release, or escape* is sudden and accidental"—is on the discharge, not the damage.[95] Such

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93. *See, e.g.*, Transamerica Ins. Co. v. Duro Bag Mfg. Co., 50 F.3d 370, 372-73 (6th Cir. 1995) (construing Kentucky law); Cincinnati Ins. Co. v. Flanders Elec. Motor Serv., Inc., 40 F.3d 146, 153 (7th Cir. 1994) (construing Indiana law); United States Fidelity & Guar. Co. v. Morrison Grain Co., 999 F.2d 489, 493 (10th Cir. 1993) (construing Kansas law); Smith v. Hughes Aircraft Co., 22 F.3d 1432, 1437-38 (9th Cir. 1993) (construing Arizona and California law); Aetna Casualty & Sur. Co. v. General Dynamics Corp., 968 F.2d 707, 710 (8th Cir. 1992) (construing Missouri law); Hartford Accident & Indem. Co. v. U.S. Fidelity & Guar. Co., 962 F.2d 1484, 1492 (10th Cir.) (construing Utah law), *cert. denied sub nom.* El Paso Natural Gas Co. v. Hartford Accident & Indem. Co., 506 U.S. 955 (1992); Northern Ins. Co. of N.Y. v. Aardvark Assoc., Inc., 942 F.2d 189, 193 (3d Cir. 1991) (construing Pennsylvania law); A. Johnson & Co. v. Aetna Casualty & Sur. Co., 933 F.2d 66, 72 (1st Cir. 1991) (construing Maine law); United States Fidelity & Guar. Co. v. Star Fire Coals, Inc., 856 F.2d 31, 34 (6th Cir. 1988) (construing Kentucky law). *But see* New Castle County v. Hartford Accident and Indem. Co., 933 F.2d 1162, 1193-99 (3d Cir. 1991) (construing Delaware law).

94. *See supra* note 30 and accompanying text for the definition of "occurrence" in the standard CGL policy.

95. *See, e.g., Hartford Accident & Indem.*, 962 F.2d at 1490-92; *New Castle County*, 933 F.2d at 1199-1202; Kerr-McGee Corp. v. Admiral Ins. Co., 905 P.2d 760, 764 (Okla. 1995); Queen City Farms, Inc. v. Central Nat'l Ins. Co. of Omaha, 882 P.2d 703, 724-25 (Wash. 1994). *But see* Joy Technologies, Inc. v. Liberty Mut. Ins. Co., 421 S.E.2d 493, 499-500 (W. Va. 1992) (limiting the effect of the pollution exclusion to a mere clarification of the definition of "occurrence" based on representations made by the insurance industry to regulators concurrent with the introduction of the

courts conclude that this interpretation is supported by the language of the exception, and by a desire to afford the pollution exclusion independent operative effect apart from the occurrence definition.

C. What is the Relevant "Discharge, Dispersal, Release or Escape?"

Courts which conclude that the occurrence definition and the pollution exclusion are not co-extensive generally agree that the focus of the occurrence definition is on the damages and the focus of the pollution exclusion is on the discharge. However, these courts remain in disagreement as to the relevant "discharge, dispersal, release or escape" for purposes of the applicability of the "sudden and accidental" analysis.

This fact-intensive question most commonly arises in the scenario where a policyholder intentionally discharged waste into a landfill, but assumed that the landfill was properly designed and would not pollute the environment. Insurers urge that the relevant "discharge, dispersal, release or escape" is the disposal of waste *into the landfill*—a discharge which was clearly intended and therefore not within the scope of the "sudden and accidental" exception to the pollution exclusion. Policyholders, however, argue that the relevant "discharge, dispersal, release or escape" is the one which was the proximate cause of the damage—the release of contaminants *from the landfill*, such release being unintended and unexpected.[96] As with the definition of "sudden," courts are split on this interpretative issue as well.[97]

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clause). *See infra* notes 118-27 and accompanying text for a discussion of such representations.

96. For the landfill scenario, this question generally only has relevance in jurisdictions which have concluded that "sudden" has no temporal component of abruptness. Otherwise, the "sudden and accidental" exception to the pollution exclusion clause would apply to *neither* discharge: The disposal of waste into the landfill is not accidental, and the migration of contamination from the landfill is generally not abrupt, but gradual.

97. *See, e.g.*, St. Paul Fire & Marine Ins. Co. v. Warwick Dyeing Corp., 26 F.3d 1195, 1204-05 (1st Cir. 1994) (rejecting the policyholder's position as "merely an attempt to recast the damages . . . as a separate discharge."); Patz v. St. Paul Fire & Marine Ins. Co., 15 F.3d 699, 702-03 (7th Cir. 1994) (holding that, where the insured buried barrels of paint sludge, the relevant release was not the dumping of the barrels, but the subsequent leaking of sludge from the barrels after they were buried); Broderick Inv. Co. v. Hartford Accident & Indem. Co., 954 F.2d 601, 606-08 (10th Cir.) (holding that the relevant discharge was the disposal of waste into containment ponds as opposed to the release of contamination from the containment pond), *cert. denied*, 506 U.S. 865 (1992); Queen City Farms, Inc. v. Central Nat'l Ins. Co. of Omaha, 882 P.2d 703, 718-19 (Wash. 1994) (holding that the relevant release is discharge of pollutants from the landfill).

In those jurisdictions which recognize a temporal component to "sudden," a different interpretative dispute arises as to the relevant discharge for purposes of the "sudden and accidental" exception. In such cases, policyholders have sought to avoid the harshness of the temporal interpretation by arguing that although the damage occurred gradually over many years, each individual "discharge, dispersal, release or escape" happened abruptly, and therefore the "sudden and accidental" exception to the pollution exclusion is applicable and operates to restore coverage for the damages arising out of each of these individual discharges.[98] The majority of courts which have considered the issue have refused to apply such a spill-by-spill analysis, reasoning that a specific point in time when an individual discharge occurred can almost always be identified, so that such an interpretation would render the temporal component of "sudden" completely ineffective.[99]

D. Unexpected and Unintended From Whose Point of View?

Whether or not a jurisdiction affords "sudden" a temporal component meaning "abrupt," in order for coverage to be available under the "sudden and accidental" exception to the pollution exclusion clause, the discharge must at least be "unexpected and unintended." The question remains, unexpected and unintended from whose point of view? The insured? The insured's predecessor in interest? The insured's third party waste contractor?

In the scenarios in which the insured's predecessor in interest intentionally polluted, or in which the insured had entrusted waste to a third party contractor, the answer to this question may be determinative. Insurers argue that the discharge must be

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98. Such an argument is completely reasonable, especially in light of the distinction made between the focus of the occurrence definition (on the damages—which usually result from cumulative effects over a period of many years) and the focus of the pollution exclusion (on the discharge—which is more likely to happen abruptly).

99. *See* Quaker State Minit-Lube, Inc. v. Fireman's Fund Ins. Co., 52 F.3d 1522, 1529 (10th Cir. 1995); Bureau of Engraving, Inc. v. Federal Ins. Co., 5 F.3d 1175, 1177-78 (8th Cir. 1993) ("[U]nder that theory all releases would be sudden, and the 'sudden and accidental' exception essentially would swallow the 'rule' of the pollution exclusion.") (citations omitted); Ray Indus., Inc. v. Liberty Mut. Ins. Co., 974 F.2d 754, 766-69 (6th Cir. 1992) ("[U]nder this theory, *all* releases would be sudden; one can always isolate a specific moment at which pollution actually enters the environment."); American Motorists Ins. Co. v. ARTRA Group, Inc., 659 A.2d 1295, 1308-09 (Md. 1995); Nashua Corp. v. First State Ins. Co., 648 N.E.2d 1272, 1275 (Mass. 1995). Perhaps these observations are simply another reason why no temporal component should be read into the word "sudden" in the pollution exclusion—because reasonable interpretations of the applicability of the term render the temporal component ineffective.

unexpected and unintended from the standpoint of the predecessor in interest or the third party whose actions are more closely associated with the discharge. Policyholders argue that the discharge must be unexpected or unintended from the standpoint of the insured, advocating consistency between the pollution exclusion and the definition of occurrence. Once again, as with most other disputes surrounding the pollution exclusion, courts are split as to the correct interpretation.[100]

III. DRAFTING AND REGULATORY HISTORY OF THE STANDARD CGL POLICY AND THE POLLUTION EXCLUSION

General liability insurance was first widely issued in the late nineteenth century, with each insurer using its own policy language.[101] In the 1930's, the insurance industry began drafting standard policy language, a process which culminated in 1941 with the introduction of the first standard CGL policy.[102] The process of drafting standard policy language, which continues to this day, is coordinated through an industry service organization to which individual insurance companies subscribe.[103] The organization which performs this function today is called the Insurance Services Office, Inc. (the "ISO").[104] The predecessor organizations to the ISO were the Insurance Rating Board (the "IRB") and the Mutual Insurance Rating Bureau (the "MIRB").[105]

Use of standard policy language affords several advantages to insurers including elimination of costs of negotiating with individual policyholders, predictability and consistency in judicial interpretations, and facilitation of reinsurance and claims adjusting.[106] This cooperation among insurers for standard policy lan-

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100. *See, e.g., Warwick Dyeing*, 26 F.3d at 1202 n.3 (noting the split of authority and assuming without deciding that the relevant point of view is that of the insured); Morton Int'l, Inc. v. General Accident Ins. Co., 629 A.2d 831, 875 (N.J. 1993) (holding that the pollution exclusion precludes coverage only for discharges expected or intended by the insured), *cert. denied*, 114 S. Ct. 2764 (1994); Powers Chemco, Inc. v. Federal Ins. Co., 548 N.E.2d 1301, 1302 (N.Y. 1989) (holding that the pollution exclusion precludes coverage for intentional conduct of insured's predecessor in interest).

101. *See* Reiter et al., *supra* note 35, at 1178 n.55.

102. *Id.*

103. *Id.*

104. CARTER & MEYER, *supra* note 25, § 3.1, at 27. The ISO describes itself as "a nonprofit corporation that provides information about the property/casualty insurance business, including statistical and actuarial information. ISO also provides advisory policy forms and a variety of related services." ISO REPORT, *supra* note 19, at ii.

105. CARTER & MEYER, *supra* note 25, § 3.1, at 27.

106. *Id.* (citing David B. Goodwin, Review Essay, *Disputing Insurance Coverage Disputes*, 43 STAN. L. REV. 779, 782-83 (1991)).

guage is possible because the insurance industry, since 1948, has enjoyed a congressional exemption from most federal antitrust prohibitions.[107]

The first standard form CGL policy was introduced in the United States in 1941 and covered damages caused by an "accident."[108] Although undefined in the policy, "accident," a term adopted from automobile liability policies, was generally thought of as a "boom" event where the cause and effect (damages) happened simultaneously.[109] By the 1960's, the nature of business liabilities had begun to change, spurred on by developing tort law in areas such as products liability, where there is often a latency period between the conduct and damages resulting therefrom.[110] In order to accommodate these new species of liabilities, courts began to interpret "accident" more expansively to encompass continuous or repeated exposure to conditions, thereby increasing insurer exposure for such claims.[111]

In response to this changing nature of business liabilities, insureds began to demand broader coverage options and insurers such as Lloyd's of London responded.[112] Faced with international competition and adverse judicial decisions, the insurance industry responded with the introduction of a new occurrence-based CGL policy in 1966.[113]

The insurance industry continually represented the change as a major expansion of coverage, noting particularly that the revised policy covered gradual polluting events. In seeking approval for the policy language from state regulatory authorities, the MIRB explained:

> Coverage has been broadened to an "occurrence" basis which is defined in the jacket. The definition reinforces the intent that the injury be fortuitous from the insured's standpoint and *by the addition of coverage for "injurious exposure to conditions" eliminates the connotation of suddenness previously intended as respects coverage on an "accident" basis.*[114]

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107. *See* McCarran-Ferguson Act § 2(b), 59 Stat. 33, 34 (1945) (codified as amended at 15 U.S.C. § 1012(b) (1994)).

108. Spracker et al., *supra* note 50, at 10067.

109. *Id.* A typical accident-based policy of that era would have provided: "[T]he insurer agrees with the insured . . . to pay, on behalf of the insured, all sums which the insured shall become legally obligated to pay as damages because of . . . injury to or destruction of property, including loss of use thereof, *caused by accident.*" Reiter et al., *supra* note 35, at 1187 n.92 (first and third alterations in original) (emphasis added) (citations omitted).

110. Spracker et al., *supra* note 50, at 10067.

111. *Id.*

112. *Id.*

113. *Id.*

114. Morton Int'l, Inc. v. General Accident Ins. Co., 629 A.2d 831, 852 (N.J.

At the time of the adoption of the occurrence-based CGL form, a memorandum entitled *Summary of Broadened Coverage Under New GL Policies With Necessary Limitations to Make This Broadening Possible* was circulated internally at Liberty Mutual Insurance Company.[115] The memorandum indicated that the new CGL policy provided coverage for "gradual [damage] resulting over a period of time from exposure to the insured's *waste disposal*. Examples would be gradual adverse effect of smoke, fumes, air or stream pollution, contamination of water supply or vegetation."[116]

In 1965, an insurance industry representative, in commenting on the new occurrence-based CGL policy stated that "[i]t is in the waste disposal area that a manufacturer's basic premises-operation coverage is liberalized most substantially."[117]

In May of 1970, just four years after the change to the occurrence-based standard CGL policy, the IRB introduced the new pollution exclusion as a mandatory endorsement to the standard CGL policy.[118] By that time, most states had promulgated statutes which required that proposals for new policy language be filed with and approved by the state insurance commissioner prior to inclusion of that language in policies issued to insureds of the state.[119]

Policyholders have often pointed to representations made by the insurance industry during this regulatory approval process as evidence that the pollution exclusion was not intended to be, or at least not represented to be, a significant reduction in pollution coverage from the 1966 occurrence-based CGL policy.[120] In efforts to gain approval for the pollution exclusion, the MIRB sub-

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1993) (quoting MIRB, EXPLANATORY MEMORANDUM OF CHANGES SUBMITTED TO THE NEW JERSEY DEPARTMENT OF BANKING & INSURANCE (1966)), *cert. denied*, 114 S. Ct. 2764 (1994).

115. Joy Technologies, Inc. v. Liberty Mut. Ins. Co., 421 S.E.2d 493, 498 (W. Va. 1992).

116. *Joy Technologies*, 421 S.E.2d at 498.

117. George Pendygraft et al., *Who Pays for Environmental Damage: Recent Developments in CERCLA Liability and Insurance Coverage Litigation*, 21 INDIANA L. REV. 117, 141-42 & n.106 (1988) (quoting G.L. Bean, Assistant Secretary, Liberty Mut. Insurance Company, *New Comprehensive Guaranty and Automobile Program, The Effects on Manufacturing Risks*, paper presented at Mutual Insurance Technical Conference 6 (1965)).

118. Soderstrom, *supra* note 31, at 766 & n.19.

119. *See, e.g.*, MINN. STAT. ANN. § 70A.06, subd. 2 (West 1986); N.J. STAT. ANN. § 17:29AA-6 (West 1994); OHIO REV. CODE ANN. § 3937.03(A) (Anderson 1989); PA. STAT. ANN. tit. 40, § 477(b) (1992).

120. *See* Salisbury, *supra* note 65.

mitted a now infamous explanatory memorandum to state insurance commissioners, which read:

> Coverage for pollution or contamination is not provided in most cases under present policies because the damages can be said to be expected or intended and thus are excluded by the definition of occurrence. The above exclusion clarifies this situation so as to avoid any questions of intent. Coverage is *continued for pollution or contamination caused injuries when the pollution or contamination results from an accident.*[121]

The same explanation was submitted to the appropriate regulatory authorities of most states.[122]

The first sentence of the explanation is quite curious: "Coverage for pollution or contamination is not provided in most cases under *present* policies because the damages can be said to be expected or intended and thus are excluded by the definition of occurrence." The then-present policy was the occurrence-based policy introduced in 1966 which was represented by the insurance industry at the time as a major *expansion* of coverage, particularly in the area of pollution.[123]

The second sentence of the explanation, "[the pollution] exclusion *clarifies* this situation," clearly implies that the pollution exclusion represented no change in coverage—simply a *clarification* of the then-current coverage afforded under the definition of occurrence.

The third sentence of the explanation provides that "[c]overage is continued for pollution or contamination caused injuries when the pollution or contamination results from an accident." This suggests that the then-current coverage for pollution damages *continues*, qualified only by the requirement that the damage

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121. Sheldon Hurwitz & Dan D. Kohane, *The Love Canal—Insurance Coverage for Environmental Accidents*, 50 INS. COUNS. J. 378, 379 (1983).

122. *See* Federated Mut. Ins. Co. v. Botkin Grain Co., 64 F.3d 537, 541 (10th Cir. 1995) (Kansas Insurance Commissioner); New Castle County v. Hartford Accident & Indem. Co., 933 F.2d 1162, 1198 (3d Cir. 1991) (Pennsylvania Commissioner of Insurance); Dimmitt Chevrolet v. Southeastern Fidelity Ins. Corp., 636 So. 2d 700, 714 (Fla. 1993) (Overton, J., dissenting from order denying rehearing) (Florida Department of Insurance); Anderson v. Minnesota Ins. Guar. Ass'n, 534 N.W.2d 706, 708 (Minn. 1995) (Minnesota Insurance Commissioner); Morton Int'l, Inc. v. General Accident Ins. Co., 629 A.2d 831, 851 (N.J. 1993) (New Jersey Department of Insurance), *cert. denied*, 114 S. Ct. 2764 (1994); Joy Technologies, Inc. v. Liberty Mut. Ins. Co., 421 S.E.2d 493, 499 (W. Va. 1992) (West Virginia Insurance Commissioner); Reiter et al., *supra* note 35, at 1200-02 (Ohio Department of Insurance). *See also* Letter from R. Stanley Smith, Manager, IRB, to Mr. Emory Lipscomb, Rating Deputy, Georgia Insurance Department, June 10, 1979, *reproduced in* Claussen v. Aetna Casualty & Sur. Co., 676 F. Supp. 1571, 1583 app. B (S.D. Ga. 1987), *rev'd*, 888 F.2d 747 (11th Cir. 1989).

123. *See supra* notes 113-17 and accompanying text for a discussion of the 1966 revision to the CGL policy.

result from an *accident*. However, the word "accident" was already part of the definition of "occurrence," so it may seem that no additional showing need be made by policyholders beyond proving an "occurrence" in order to make out a valid claim for coverage of pollution damages under the standard CGL policy.

As further evidence that the insurance industry intended the pollution exclusion as merely a clarification of the occurrence definition, an underwriter's handbook described the purpose of the clause as follows:

> In one important respect, the exclusion simply reinforces the definition of occurrence. That is, the policy states that it will not cover claims where the "damage was expected or intended" by the insured and the exclusion states, in effect, that the policy will cover incidents which are sudden and accidental—unexpected and not intended.[124]

Clearly, the official explanation of the insurance industry in support of the pollution exclusion would lead a reasonable regulator, and indeed a reasonable policyholder, to conclude that no substantial reduction in coverage was intended. There is evidence in the response of the regulators that they did indeed so conclude.

After considering insurance industry explanations as to the scope of the pollution exclusion, in approving the clause, the Kansas Insurance Commissioner replied that "although we are in agreement that pollution and contamination need some type of outlines established, it should be recognized by the [insurance] industry that there can be purely accidental pollution and there should be coverage provided for the insured that is not at fault."[125]

Similarly, the West Virginia Insurance Commissioner, in reliance upon insurance industry representations as to the scope of the pollution exclusion, gave his approval of the clause with an order that stated:

> (1) The said companies and rating organizations have represented to the Insurance Commissioners, orally and in writing, that the proposed exclusions . . . are merely clarifications of existing coverage as defined and limited in the definitions of the term "occurrence," contained in the respective policies to which said exclusions would be attached;
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> (2) To the extent that said exclusions are mere clarifications of existing coverage, the Insurance Commissioner finds that there is no objection to the approval of such exclusions.[126]

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124. Hurwitz & Kohane, *supra* note 121, at 379 (citations omitted).
125. *Botkin Grain*, 64 F.3d at 541 (alteration in original).
126. *Joy Technologies*, 421 S.E.2d at 499 (alteration in original).

Further, in submitting the pollution exclusion clause to state regulators for approval, the insurance industry did not apply for any corresponding premium reduction for what it now represents to have been a significant curtailment in coverage.[127]

After the clause was approved by the respective state insurance commissioners, it was universally included by insurers in CGL policies issued to governmental and business insureds for the next decade and a half until it was replaced by the absolute pollution exclusion in 1986.[128]

IV. ARGUMENTS FOR INTERPRETATION IN FAVOR OF COVERAGE

Over the last several years, and especially in 1995, insurers have increasingly garnered favorable court rulings on the interpretation of the pollution exclusion in jurisdictions throughout the country.[129] This comment is in response to that trend, in an effort to develop arguments which may be used to influence jurisdictions which have yet to decide the issue. This Part reviews the classic legal theories supporting a pro-coverage interpretation of the pollution exclusion—contra insurer, estoppel and public policy—yet does so in light of modern movements in contract law as well as recent developments in the insurance industry.

A. The Contra Insurer and Reasonable Expectations Doctrines

There are two well established and closely related rules of insurance policy construction, both of which point to interpretation in favor of coverage. They are the contra insurer doctrine and the reasonable expectations doctrine. Contra insurer is essentially a corollary of the *contra proferentum* rule. The rule holds that any ambiguities in an insurance policy are to be re-

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127. Morton Int'l, Inc. v. General Accident Ins. Co., 629 A.2d 831, 872-73 (N.J. 1993), *cert. denied*, 114 S. Ct. 2764 (1994).

128. *Morton*, 629 A.2d at 831. The pollution exclusion was approved in almost every state—New Hampshire being one of the rare exceptions. Reiter et al., *supra* note 35, at 1168 & n.18.

129. Indeed, the A.M. Best Company, in observation of "favorable emerging case law," has lowered its "insurers' liability factor," which is an estimate of the proportion of PRP liability that will be borne by insurers, from 50% to 40%. BEST REPORT, *supra* note 36, at 9.

The insurance industry has been accused of manipulating the development of important judicial precedent, especially in environmental claims cases. *See* Roger Parloff, *Rigging the Common Law*, AM. LAW., Mar. 1992, at 74 (cataloging reports of insurers making settlement offers in exchange for agreements to forgo appeal of pro-insurer decisions or to join in a petition for vacature or depublication of pro-policyholder decisions). Perhaps this tactic is a factor in the recent development of "favorable emerging case law."

solved against the drafter of the policy—the insurer.[130] The contra insurer rule is the law in at least forty-six states,[131] and is especially applicable to exclusionary clauses.[132]

The second rule is the reasonable expectations doctrine, which holds that an insurance policy should be interpreted in accordance with the reasonable expectations of the insured.[133] The reasonable expectations doctrine applies irrespective of whether the language in the policy is ambiguous or unambiguous—it simply asks: "Would a reasonable insured in this position expect coverage?"[134] The court may look to extrinsic evidence to determine if the reasonable expectations of the insured were influenced by misleading statements on the part of the insurer.[135] At least thirty-eight states recognize the reasonable expectations doctrine.[136]

There are several important justifications for these pro-policyholder interpretation canons. The first is that insurance policies are essentially adhesion contracts—the nonnegotiable policy language is drafted by the insurer and the insured is in no position to bargain.[137] Secondly, these canons give insurers an incentive to draft clear and unmistakable policy language, which, in turn, serves to reduce claim litigation.[138] Finally, because these canons turn policy language interpretation into a question of law, coverage litigation can more often be resolved at the summary judgement stage, avoiding time-consuming and expensive discovery into the facts surrounding the intent of the parties.[139]

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130. *See* Outboard Marine Corp. v. Liberty Mut. Ins. Co., 607 N.E.2d 1204, 1217 (Ill. 1992); JOHN A. APPLEMAN & JEAN APPLEMAN, 13 INSURANCE LAW AND PRACTICE § 7401, at 197 (1976) ("It has been almost the unanimous holding of all courts that insurance contracts must be liberally construed in favor of a policyholder . . . wherever possible, and strictly construed against the insurer in order to afford the protection which the insured was endeavoring to secure when he applied for the insurance.").

131. See ZULKEY, *supra* note 25, § 3.05, at 3-5. For a list of these states and contra insurer case law, see *id.* at app. 3A.

132. New York v. Blank, 27 F.3d 783, 789 (2d Cir. 1994) ("[A]n insurer must establish that the exclusion is stated in clear and unmistakable language [and] is subject to no other reasonable interpretation . . . .") (quoting Continental Casualty Co. v. Rapid-American Corp., 609 N.E.2d 506, 512 (N.Y. 1993)); *Outboard Marine*, 607 N.E.2d at 1217.

133. *See* ZULKEY, *supra* note 25, § 3.06, at 3-6.

134. *Id.*

135. *Id.* § 3.09, at 3-11.

136. *Id.* § 3.08, at 3-10. For a list of these states and the relevant case law, see *id.* at app. 3B.

137. *Outboard Marine*, 607 N.E.2d at 1217; Goodwin, *supra* note 106, at 787; COUCH, *supra* note 52, § 15:78, at 382-87.

138. Goodwin, *supra* note 106, at 787.

139. *Id.* at 787-88. It is not inequitable that this question of law would most

It would seem that, using these pro-insured rules of policy interpretation, courts would uniformly interpret the pollution exclusion in favor of coverage. However, there are two arguments commonly raised by insurers in an effort to preclude applicability of these doctrines to pollution exclusion disputes—the plain meaning rule and the sophisticated insured doctrine. As discussed below, in light of modern movements in contract law and recent developments in the insurance industry, these arguments must fail.

1. The Fallacy of the Plain Meaning Rule

The conditions precedent for application of the contra insurer doctrine and the reasonable expectations doctrine, are, respectively, that the policy language be ambiguous and that the expectation of the insured is reasonable. However, much of the evidence which demonstrates the existence of these conditions is extrinsic to the policy, e.g., conflicting dictionary definitions,[140] drafting and regulatory history,[141] pre-existing judicial construction[142] and conflicting judicial decisions.[143] Unfortunately, some courts have simply refused to consider the extrinsic evidence, rigidly applying the plain meaning rule, and holding that if the words in the policy are "unambiguous" on their face, the court is simply unable to entertain extrinsic evidence, regardless of its probative value or persuasiveness.[144]

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often allow summary judgement to be granted in favor of the insured. When a sizable claim is the subject of litigation, an insurer often has no incentive to settle and every incentive to prolong the litigation. This is so because during the pendency of the litigation, the insurer may make more money through investment return on the withheld claim then it spends in disputing it. *Id.* at 787-88 & n.46.

140. *See supra* notes 53-54 and accompanying text.

141. *See supra* Part III.

142. *See supra* Part II.A.3.

143. *See supra* notes 53-100 and accompanying text. The existence of conflicting judicial decisions is generally accepted as strong evidence of ambiguity. *See* COUCH, *supra* note 52, § 15:84, at 419 ("The fact that courts of the several jurisdictions have arrived at different constructions as to the meaning of the words in a provision or exclusion of a policy, and even in some instances have taken almost opposite views, is some indication that the terms are ambiguous."). *See also* Just v. Land Reclamation, Ltd., 456 N.W.2d 570, 578 (Wis. 1990). The *Just* court stated:

> [T]he fact that substantial conflicting authority exists with respect to the "correct" interpretation of the exclusionary terms merely serves to strengthen the conclusion that the terms are susceptible to more than one meaning, and thus ambiguous . . . . [T]his type of comprehensive debate dispels the insurer's contention that the exclusionary language is clear.

Just, 456 N.W.2d at 578 (citations omitted).

144. *See, e.g.*, Federated Mut. Ins. Co. v. Botkin Grain Co., 64 F.3d 537, 541 (10th Cir. 1995); Transamerica Ins. Co. v. Duro Bag Mfg. Co., 50 F.3d 370, 373 (6th Cir. 1995); Cincinnati Ins. Co. v. Flanders Elec. Motor Serv., Inc., 40 F.3d 146, 153

An early statement of the plain meaning rule can be found in an 1843 English case:

> [W]here the words of any written instrument are free from ambiguity in themselves, . . . such instrument is always to be construed according to the strict, plain, common meaning of the words themselves; . . . [and] evidence *dehors* the instrument for the purpose of explaining it according to the surmised or alleged intention of the parties to the instrument is utterly inadmissable.[145]

However, the plain meaning rule has fallen out of favor with modern courts and contract scholars.[146]

First of all, the rule presumes that the plain meaning of words in a contract, and whether or not such words are ambiguous, can be readily ascertained simply from an examination of the instrument itself. In interpreting the pollution exclusion, the Supreme Court of Ohio made that presumption when it stated that because the intent of the parties was evident from "clear and unambiguous" policy language, the court refused to "resort to construction of that language."[147] On such logic, the eminent contract scholar, Professor Corbin, has remarked:

> It is sometimes said, in a case in which the written words seem plain and clear and unambiguous, that the words are not subject to interpretation or construction. One who makes this statement has of necessity already given the words an interpretation—the one that is to him plain and clear; and in making the statement he is asserting that any different interpretation is "perverted" and untrue.[148]

Indeed, Oliver W. Holmes has observed that "[a] word is not crystal, transparent and unchanged; it is the skin of a living thought and may vary greatly in color and content according to the circumstances and the time in which it is used,"[149] and Pro-

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(7th Cir. 1994); Dimmitt Chevrolet, Inc. v. Southeastern Fidelity Ins. Corp., 636 So. 2d 700, 705 (Fla. 1993); Lumbermens Mut. Casualty v. Belleville Indus., Inc., 555 N.E.2d 568, 573 (Mass. 1990); Upjohn Co. v. New Hampshire Ins. Co., 476 N.W.2d 392, 396 n.6 (Mich. 1991); Kerr-McGee Corp. v. Admiral Ins. Co., 905 P.2d 760, 764 (Okla. 1995).

145. Margaret N. Kniffin, *A New Trend in Contract Interpretation: The Search for Reality as Opposed to Virtual Reality*, 74 OR. L. REV. 643, 644 n.2 (1995) (quoting Attorney-General v. Shore, 11 Sim. 592, 615-31 (1843), *reprinted in* 59 Eng. Rep. 1002, 1021 (1906)).

146. *See generally* Kniffin, *supra* note 145 (discussing the trend of rejection of the plain meaning rule as unrealistic). Professor Kniffin is responsible for revisions to the contract interpretation volume of Corbin on Contracts. *Id.* at 643 n.*.

147. Hybud Equip. Corp. v. Sphere Drake Ins. Co., 597 N.E.2d 1096, 1102 (Ohio 1992) (citations omitted), *cert. denied*, 507 U.S. 987 (1993).

148. JOHN EDWARD MURRAY, JR., MURRAY ON CONTRACTS § 86, at 406 (1990) (quoting Authur L. Corbin, *The Interpretation of Words and the Parol Evidence Rule*, 50 CORNELL L. REV. 161, 171-72 (1965)).

149. MURRAY, *supra* note 148, § 86, at 407 (quoting Towne v. Eisner, 245 U.S.

fessor Farnsworth, Reporter for the Restatement (Second) of Contracts, wonders whether "a word has any meaning at all when divorced from the circumstances in which it is used."[150]

Not only is the plain meaning rule based on an unrealistic presumption which has been rejected by twentieth century contract scholars, but that presumption is then used to preclude consideration of the very evidence that may reveal its fallacy. Modern contract scholars uniformly disfavor this mechanical and ill-advised preclusion of extrinsic evidence.[151] The more modern view favors consideration of extrinsic evidence of the circumstances of the making of the contract as part of the interpretative process, without any finding of "ambiguity" as a condition precedent.[152] This is the view adopted by the Restatement (Second) of Contracts, Article 2 of the Uniform Commercial Code, and the United Nations Convention on Contracts for the International Sale of Goods.[153]

418, 425 (1918)).

150. E. ALLAN FARNSWORTH, II FARNSWORTH ON CONTRACTS § 7.10, at 256 (1990) (citing E. Allan Farnsworth, *"Meaning" in the Law of Contracts*, 76 YALE L.J. 939, 940-42 (1967)).

151. *See* AUTHUR L. CORBIN, CORBIN ON CONTRACTS §§ 542-542A, at 100-29 (1960 & Supp. 1994). A rigid application of the plain meaning rule "should be subject to constant attack and disapproval." *Id.* § 542, at 108-10. *See also* Pacific Gas & Elec. Co. v. G. W. Thomas Drayage & Rigging Co., 442 P.2d 641 (Cal. 1968) (Traynor, C.J.). The court stated:

> A rule that would limit the determination of the meaning of a written instrument to its four-corners merely because it seems to the court to be clear and unambiguous, would either deny the relevance of the intention of the parties or presuppose a degree of verbal precision and stability our language has not attained.

Pacific Gas & Elec., 442 P.2d at 644.

152. *See* FARNSWORTH, *supra* note 150, § 7.10, at 255-56 (citations omitted). Farnsworth states:

> The overarching principle of contract interpretation is that the court is free to look to all the relevant circumstances surrounding the transaction. This includes all writings, oral statements, and other conduct by which the parties manifested their assent, together with any prior negotiations between them and any applicable course of dealing, course of performance, or usage. . . . [T]here should be no requirement that the language be ambiguous, vague, or otherwise uncertain before the inquiry is undertaken.

Id.

See also Pacific Gas & Elec., 442 P.2d at 644 (holding that the standard for admissibility of extrinsic evidence to interpret a contract was not whether language appeared "clear and unambiguous" on its face, but whether such evidence is relevant to prove a meaning to which the language is reasonably susceptible); MURRAY, *supra* note 148, § 86, at 407 ("While the interpretation process should begin with the usual and ordinary meaning of the words in a contract, courts should be willing to admit evidence that would supersede the usual meaning, e.g., evidence of trade usage.") (citations omitted).

153. Kniffin, *supra* note 145, at 649-51 (citations omitted).

In fact, it seems that influential insurance law treatises may also be recog-

In accord with this view, the Supreme Court of West Virginia relied heavily on the extrinsic evidence of the drafting and regulatory history of the pollution exclusion clause, and concluded that in light of such evidence the clause would be given effect only to the extent that it clarifies the definition of "occurrence."[154]

2. *The Fallacy of the Sophisticated Insured Argument*

Insurers also argue that commercial policyholders should not be given the benefit of contra insurer and reasonable expectations doctrines because they are "sophisticated" insureds that are in no need of the judicial protection which may be afforded to individual consumers.[155] As appealing as this argument may seem in theory, in fact, whether the insured is a residential homeowner or a multinational manufacturer, the insured is presented with standard non-negotiable policy language on a take-it-or-leave-it basis.[156] The use of the standard CGL policy across the entire insurance industry effectively robs even "sophisticated" insureds of any benefit which may be derived from competition among insurers for more favorable language. In fact, even corporate policyholders rarely receive a copy of the policy until after the premium is paid.[157] If a corporate insured has any bargaining power at all, such power would normally be exercised in order to increase coverage limits, not to dicker about policy language.[158] Indeed, the very purpose of the regulatory approval

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nizing the more modern view in recent revisions. *See* APPLEMAN, *supra* note 130, § 7386, at 38 (Supp. 1995) ("In deciding whether an ambiguity in an insurance policy exists, the court must not consider the policy in a vacuum but instead is required to consider the particular factual setting in which the policy was issued.").

154. Joy Technologies, Inc. v. Liberty Mut. Ins. Co., 421 S.E.2d 493, 499-500 (W. Va. 1992).

155. *See, e.g.*, Smith v. Hughes Aircraft Co., 22 F.3d 1432, 1437 (9th Cir. 1993) ("Hughes is not an unsophisticated consumer . . . ."); Outboard Marine Corp. v. Liberty Mut. Ins. Co., 607 N.E.2d 1204, 1218 (Ill. 1992) ("The insurers argue that [contra insurer] should not apply here because [the insured] is a large corporation, sophisticated and counseled in insurance matters."). *See also* APPLEMAN & APPLEMAN, *supra* note 130, § 7403, at 301 (The contra insurer doctrine "need not be strictly adhered to in instances where one large corporation and one large insurance company both advised by competent counsel do business with each other.").

156. *Outboard Marine*, 607 N.E.2d at 1217-18 ("The insurance industry is powerful and closely knit. . . . Any insured, whether large and sophisticated or not, must enter into a contract with the insurer which is written according to the insurer's pleasure by the insurer.").

157. Nancy Ballard & Peter Manus, *Clearing Muddy Waters: Anatomy of the Comprehensive General Liability Pollution Exclusion*, 75 CORNELL L. REV. 610, 621 (1990).

158. Goodwin, *supra* note 106, at 797.

process for standard policy language is so that the state can negotiate with the insurance industry on behalf of policyholders who never get that chance.[159]

The limited availability and high cost of pollution coverage in today's insurance market aptly demonstrates the reality of the superior bargaining power of the insurers, regardless of the character of the insured.[160] A recent study by the United States General Accounting Office (the "GAO") revealed that most hazardous waste management facilities report great difficulty in obtaining pollution insurance, with nearly half of those who seek pollution insurance being denied.[161] The study also showed that today's pollution coverage business is dominated by one insurer—National Union Fire Insurance Company—which corners 77% of the market.[162] The median premium charged is $22 per $1,000 of annual aggregate coverage,[163] translating into an average annual premium of $22,000 to $176,000.[164]

Additional evidence of the non-competitive nature of the pollution coverage market is found in the recently settled massive insurance antitrust litigation.[165] Suit was brought by twenty state attorneys general against four U.S. insurers—Hartford, Allstate, Aetna and CIGNA—two industry trade associations including the ISO, and various foreign and domestic reinsurers.[166] The defendants were charged with conspiracy in violation of section one of the Sherman Act.[167] The complaint al-

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159. *See* Morton Int'l, Inc. v. General Accident Ins. Co., 629 A.2d 831, 848 (N.J. 1993) ("The [insurance] industry's presentation and characterization of the standard pollution-exclusion clause to state regulators constituted virtually the only opportunity for arms-length bargaining by interests adverse to the industry, insureds having virtually no choice at all but to purchase the industry-wide standard CGL policy."), *cert. denied*, 114 S. Ct. 2764 (1994).

160. Today, pollution coverage is generally provided under Environmental Impairment Liability ("EIL") policies, purchased separately to supplement the coverage provided by the standard CGL policy. *See* CARTER & MEYER, *supra* note 25, § 4.3, at 48-51.

161. GAO, HAZARDOUS WASTE—AN UPDATE ON THE COST AND AVAILABILITY OF POLLUTION INSURANCE 23 (1994) [hereinafter COST AND AVAILABILITY OF POLLUTION INSURANCE].

162. COST AND AVAILABILITY OF POLLUTION INSURANCE, *supra* note 161, at 20.

163. *Id.*

164. EPA regulations require that hazardous waste management facilities demonstrate annual aggregate pollution coverage of $2 million to $8 million depending upon the type of facility. COST AND AVAILABILITY OF POLLUTION INSURANCE, *supra* note 161, at 11 (citing 40 C.F.R. § 264.147 (1995)).

165. *See Insurance Companies Settle Multistate Conspiracy Charges*, 67 Antitrust & Trade Reg. Rep. (BNA) 434, 434 (1994) [hereinafter *Insurance Companies Settle*].

166. *Insurance Companies Settle*, *supra* note 165, at 434.

167. Hartford Fire Ins. Co. v. California, 113 S. Ct. 2891, 2895 (1993) (citing 15 U.S.C. § 1 (1994)).

leged that the defendants conspired, using the ISO and the London reinsurance market, to pressure other domestic insurers to change their CGL policies to conform to the policies being offered by the defendants.[168] Among the changes that the defendants allegedly conspired to enforce was the complete elimination from the market of the "sudden and accidental" pollution exclusion in favor of the absolute pollution exclusion.[169] Although the insurance industry has been granted qualified immunity from federal antitrust laws under section 2(b) of the McCarran-Ferguson Act,[170] the Supreme Court held that such immunity does not extend to most of the conduct alleged in the complaint by the attorneys general, and allowed the suit to proceed.[171] After the adverse Supreme Court ruling, the industry settled with the states.[172] In the settlement, which was reached in October of 1994, the defendants agreed to pay $36 million and to effectuate major changes in the industry.[173]

In light of these realities of the superior bargaining power of the insurance industry in dictating standard policy language, the justifications for the contra insurer and reasonable expectations doctrines remain strongly applicable even in the case of the "sophisticated" insured.

B. Estoppel

Given the consistent representations by the insurance industry that the pollution exclusion was merely a clarification of the occurrence definition and the lack of any indication by the industry that the exclusion was intended to effect a significant reduction in coverage, there are only two possible explanations for the industry's behavior: the industry intentionally misled regulators in 1970 or the industry did not intend, in 1970, that the pollution

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168. *Hartford Fire*, 113 S. Ct. at 2895-97. Specifically, the complaints alleged that the ISO agreed to stop providing vital actuarial and rating information support services for standard policy forms that contained language disfavored by the defendants, and that the foreign reinsurers agreed to refuse to reinsure policies written on such forms. *Id.* at 2897-99.

169. *Id.* at 2897-99. The complaint also alleged that the defendants conspired to pressure insurers to write exclusively claims-made CGL policies and eliminate occurrence-based CGL policies. *Id.* at 2896. Such a change would also effectively reduce coverage for damages from polluting events due to the long latency period often associated with such damages.

170. 15 U.S.C. § 1012(b) (1994).

171. *Hartford Fire*, 113 S. Ct. at 2895. The McCarran-Ferguson Act does not provide the insurance industry with antitrust immunity for conduct involving "boycott, coercion, or intimidation." *Id.* at 2900-01 (citing 15 U.S.C. § 1013(b) (1994)).

172. *Insurance Companies Settle*, *supra* note 166, at 434.

173. *Id.*

exclusion effect a significant reduction in coverage.

Several courts and commentators which have examined the drafting and regulatory history of the pollution exclusion have concluded that there was intentional misrepresentation by the insurance industry in 1970.[174] However, let's explore the theory that the industry did not intend, in 1970, that the pollution exclusion effect a reduction in coverage, but adopted that position post facto when the industry was faced with escalating environmental liabilities after CERCLA.

Some courts which have considered but rejected this theory have proffered that the pollution exclusion must have been intended to effect *some* reduction in coverage—it would make no sense for the insurance industry to introduce an exclusion that is co-extensive with the definition of occurrence and therefore merely superfluous and ineffective language.[175] However, commentators who have analyzed the history leading to the introduction of the pollution exclusion have offered an alternative motivation, besides coverage reduction, for the insurance industry to introduce the pollution exclusion.

In the late 1960's, there was a recent upsurge in environmental awareness, spurred on by several high profile environmental disasters including the sinking of the oil tanker *Torrey Canyon* off the coast of England and an oil drilling accident off the coast of Santa Barbara, California.[176] In 1970, the United States celebrated its first Earth Day, awakening the collective conscious of the country to environmental issues.[177] Due to the pressures precipitated by these events, the insurance industry wanted to assure that it was viewed in the eyes of the public as being "against polluters," and saw the pollution exclusion as a way to effectuate this public relations goal.[178] This theory of the industry's motivation for the introduction of the pollution exclu-

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174. *See* Claussen v. Aetna Casualty & Sur. Co., 676 F. Supp. 1571, 1573 n.4 (S.D. Ga. 1987) ("The Court finds dishonesty in the representation made to the Georgia Insurance Department in 1970 that the pollution exclusion clause would have little effect on preexisting coverage."), *rev'd on other grounds*, 888 F.2d 747 (11th Cir. 1989). *See also infra* note 189 and accompanying text for a finding of deception by the Supreme Court of New Jersey.

175. *See, e.g.*, New Castle County v. Hartford Accident & Indem. Co., 933 F.2d 1162, 1201-02 (3d Cir. 1991).

176. *See* Reiter et al., *supra* note 35, at 1167, 1194-96.

177. *Earth Day—Thousands Gather for Demonstrations, Some Ask How Long Effect Will Last*, 1 Env't Rep. (BNA) 13 (1970).

178. *See* Reiter et al., *supra* note 35, at 1168, 1195-96. *See also New Castle County*, 933 F.2d at 1197 ("According to the [insured], the insurers appended this exclusion onto their policies in order to reaffirm existing limits on pollution coverage, thus distancing themselves in the public mind from deliberate polluters.").

sion is more historically tenable than the theory that the insurance industry did intend to restrict coverage for unexpected and unintended pollution. In 1970, the insurance industry certainly could not have foreseen the imposition ten years later of broad liability for non-negligent pollution under CERCLA.[179]

Irrespective of whether the insurance industry was guilty of misrepresentation in 1970, or whether it merely did not intend, in 1970, that the pollution exclusion effect a significant reduction in coverage, the industry should now be estopped from claiming, a quarter-century later, that the pollution exclusion is more restrictive than representations made to policyholders and state regulators at the time of the introduction of the clause, because such policyholders and regulators have relied on those representations to their detriment.

The use of the estoppel theory in interpreting the pollution exclusion was introduced by the Supreme Court of New Jersey in *Morton International, Inc. v. General Accident Insurance Co.*[180] In *Morton*, the plaintiff's ("Morton") predecessor in interest had operated a mercury processing plant for over forty years, resulting in significant mercury contamination of the plant property and a nearby creek.[181] The New Jersey Department of Environmental Protection sued Morton and other defendants to compel remediation of the contaminated site.[182] Morton, in turn, sued the insurer-defendants seeking reimbursement for the remediation costs under several of the CGL policies held by Morton and its predecessors.[183] The insurers raised, among other defenses, the pollution exclusion as a bar to coverage.[184] The court concluded that, if given a literal interpretation (including a temporal component to "sudden"), the pollution exclusion would operate as a "sharp[] and dramatic[]" restriction of coverage from that previously afforded under the pre-1970 standard CGL policy.[185] However, because the insurance industry represented that the pollution exclusion was merely a "clarification" of the occurrence definition,[186] the court refused to afford the insurance industry the benefit of its misrepresentations, but would interpret

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179. *See* Claussen v. Aetna Casualty & Sur. Co., 380 S.E.2d 686, 689 n.4 (Ga. 1989).

180. 629 A.2d 831 (N.J. 1993), *cert. denied*, 114 S. Ct. 2764 (1994).

181. *Morton*, 629 A.2d at 834.

182. *Id.*

183. *Id.* at 834-35.

184. *Id.* at 847.

185. *Id.*

186. *See supra* notes 118-27 and accompanying text for the insurance industry representation of the pollution exclusion clause before state insurance regulators.

the pollution exclusion in accordance with the "objectively reasonable expectations" of the regulatory authorities who approved the clause in 1970 in reliance on the industry assurances.[187] The court stated:

> [W]e decline to enforce the standard pollution-exclusion clause as written. To do so would contravene this State's public policy requiring regulatory approval of standard industry-wide policy forms to assure fairness in rates and in policy content, and would condone the industry's misrepresentations to regulators in New Jersey and other states concerning the effect of the clause.[188]

> To describe a reduction in coverage of that magnitude as a "clarification" not only is misleading, but comes perilously close to deception. Moreover, had the industry acknowledged the true scope of the proposed reduction in coverage, regulators would have been obliged to consider imposing a correlative reduction in rates.[189]

Exercising its equitable powers, the court used the estoppel theory, based on the reasonable reliance of state regulators and insureds, to construct an interpretation of the pollution exclusion consistent with the representations made by the insurance industry in 1970.[190] The court summarized its estoppel doctrine this way:

> [W]here an insurer or its agent misrepresents, even though innocently, the coverage of an insurance contract, or the exclusions therefrom, to an insured before or at the inception of the contract, and the insured reasonably relies thereupon to his ultimate detriment, the insurer is estopped to deny coverage after a loss on a risk or from a peril actually not covered by the terms of the policy. *The proposition is one of elementary and simple justice.*[191]

As to the issue of reliance on the part of insureds, the court proffered that, once approved by the regulators, the standard

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187. *Morton*, 629 A.2d at 848.

188. *Id.*

189. *Id.* at 853.

190. Specifically, the court held that the pollution exclusion would operate to "provide coverage identical with that provided under the prior occurrence-based policy, except that the clause will be interpreted to preclude coverage in cases in which the *insured* intentionally discharges a known pollutant, irrespective of whether the resulting property damage was intended or expected." *Morton*, 629 A.2d at 875. Significantly, the court further clarified that the clause would not operate to preclude coverage in the event that the *insured's predecessor in interest* intentionally polluted. *Id.*

191. *Morton*, 629 A.2d at 873 (quoting Harr v. Allstate Ins. Co., 255 A.2d 208, 219 (N.J. 1969)) (emphasis added). For arguments in support of estoppel theory as applied to insurance contracts, see Robert E. Keeton, *Insurance Law Rights at Variance with Policy Provisions*, 83 HARV. L. REV. 961, 977-85 (1970).

CGL policy language is nonnegotiable, so insureds rely on the regulators to protect their interests.[192] Therefore, the reliance of the regulators on the representations made by the insurance industry would be imputed to insureds.[193]

Although the Supreme Court of New Jersey is the only high court which has explicitly invoked the estoppel theory in order to construe the pollution exclusion in favor of coverage, other courts have used the clause's drafting and regulatory history as extrinsic evidence of ambiguity and of the reasonable expectations of the insured, and concluded that such evidence mandates a pro-coverage construction.[194] No court has reviewed the drafting and regulatory history of the pollution exclusion clause and concluded that such history supports the interpretation urged by insurers. Courts which place a pro-insurer construction on the pollution exclusion have done so *in spite of* the regulatory and drafting history, rigidly clinging to the plain meaning rule, and refusing to consider extrinsic evidence of the intent of the parties because the court has deemed the language of the policy to be "unambiguous" on its face.[195]

Not only is such a rigid position out of date with modern contract law,[196] it is completely irrelevant to an application of estoppel theory. Estoppel is an equitable principle based on reliance and assuring justice and fairness. It is not subject to contract law concepts such as the plain meaning rule.

The Supreme Court of Minnesota, however, in construing the pollution exclusion, did consider reliance when it rejected the insured's estoppel argument. Incredibly, the court proffered that, even if insurers misrepresented the pollution exclusion clause before the Minnesota Insurance Commissioner, it was unreasonable for the Commissioner to have relied on the representations.[197] What is the converse of this proposition? That the insurance commissioner can reasonably expect insurance industry representatives to perjure themselves in commission hearings?

The Minnesota court's view notwithstanding, it would be un-

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192. *Morton*, 629 A.2d at 875.

193. *Id.* Therefore, an individual insured, in order to benefit from the court's holding in *Morton*, need not make a showing that it relied on, or even had knowledge of, the representations made by the insurance industry in 1970 regarding the pollution exclusion.

194. *See, e.g.*, Joy Technologies, Inc. v. Liberty Mut. Ins. Co., 421 S.E.2d 493, 500 (W. Va. 1992).

195. *See supra* note 144.

196. *See supra* notes 146-53 and accompanying text.

197. Anderson v. Minnesota Ins. Guar. Ass'n, 534 N.W.2d 706, 709 (Minn. 1995) (citations omitted).

conscionable to allow insurers to deny coverage for protection for which it ostensively collected premiums from policyholders based on misrepresentations made to regulatory authorities in 1970, and therefore courts should be willing to exercise their equitable powers and estop insurers from benefitting from such misrepresentations to the detriment of policyholders.

C. *Public Policy*

1. *The Fallacy of the Public Policy Arguments Against Coverage*

Insurers argue that by strictly construing the pollution exclusion clause against coverage, policyholders will take more care to avoid pollution with the knowledge that the financial responsibility for any resulting damage to the environment will be borne exclusively by the policyholder.[198] This is often referred to as controlling the "moral hazard" of pollution.[199] Often, courts which have adopted a pro-insurer interpretation of the pollution exclusion are under the mistaken impression that such an interpretation will further public policy by discouraging polluting behavior.[200]

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198. *See* Erwin E. Adler & Steven A. Broiles, *The Pollution Exclusion: Implementing the Social Policy of Preventing Pollution Through the Insurance Policy*, 19 LOY. L.A. L. REV. 1251 (1986).

199. *See* Charter Oil Co. v. American Employers' Ins. Co., 69 F.3d 1160, 1166-67 & n.2 (D.C. Cir. 1995) (using the moral hazard theory in support of a temporal interpretation of "sudden," yet conceding that abruptness "is an imperfect mechanism" for identifying intentional polluters and "presumably has little if any bearing" on controlling the moral hazard).

200. *See, e.g., Charter Oil*, 69 F.3d at 1166 (proffering that if the court allowed recovery, "insureds will be tempted . . . to engage in harm-generating (or reckless) behavior; i.e., will be subject to 'moral hazard.'"); Smith v. Hughes Aircraft Co., 22 F.3d 1432, 1437 (9th Cir. 1993) (noting that adopting a strict reading of the "sudden and accidental" exception to the pollution exclusion "further[s] public policy by excluding deliberate indifference on the part of a polluting insured."); Waste Management of Carolinas, Inc. v. Peerless Ins. Co., 340 S.E.2d 374, 381 (N.C. 1986) ("[I]f an insured knows that liability incurred by all manner of negligent or careless spills and releases is covered by his liability policy, he is tempted to diminish his precautions and relax his vigilance."); Hybud Equip. Corp. v. Sphere Drake Ins. Co., 597 N.E.2d 1096, 1103 (Ohio 1992) ("[A pro-coverage] interpretation might encourage the polluter to be less than diligent, as merely negligent acts would be covered under the policy."), *cert. denied*, 507 U.S. 987 (1993).

See especially the comments by the dissenter on the Supreme Court of Wisconsin from a pro-coverage interpretation of the pollution exclusion, overstating his case quite a bit in stating:

> *There is no longer any reason for an owner to carefully operate a dump site* because under the language of this policy as construed by the majority, all negligently caused damages are now covered, as long as the damages are not deliberate, or are unintentional, or are unexpected, even though pollution discharges from a landfill site most likely can be expected.

However, such an argument is completely inapplicable to an interpretation of the "sudden and accidental" pollution exclusion, because the clause has not been part of the standard CGL policy since 1986. Courts interpreting the pollution exclusion clause today are evaluating its applicability to the conduct of policyholders (or their predecessors in interest or their third party contractors) which took place during the relevant policy period, generally confined to the years 1970 through 1986.

Indeed, the Supreme Court of Georgia was astute in recognizing that current and future CGL policyholders are no longer operating with coverage provided under policies containing the "sudden and accidental" pollution exclusion.[201] The court stated:

> [The insurer] argues that [the pro-coverage] interpretation of the policy language contravenes public policy because it encourages the land owner to keep his head in the sand—to remain oblivious to ongoing polluting activities on his land. . . . [But] many events . . . have taken place between the date of this policy and the present lawsuit. . . . *In short, the situation has changed so that our decision [to allow coverage] is not likely to have any serious impact on prospective behavior [of policyholders].*[202]

Further, even pollution insurance covering prospective policyholder conduct is not against public policy. Quite to the contrary, a showing of financial responsibility by waste management and petroleum storage facilities is *required* by EPA regulations, which list pollution insurance as an approved compliance mechanism.[203]

In reality, insurance ultimately covers a very small fraction of an insured's environmental cleanup liabilities, creating no disincentive to diligent environmental practices. For example, a recent study by the Rand Institute for Civil Justice found that insurers reimburse PRP's for about eight percent of all Superfund-related expenditures.[204]

Even assuming that insureds received 100% reimbursement for their cleanup liabilities, in today's world, there are incentives unrelated to insurance which encourage industrial policyholders to practice environmentally sound waste management and chemical handling practices.

Most notably, not only do federal and state environmental laws

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Just v. Land Reclamation, Ltd., 456 N.W.2d 570, 579 (Wis. 1990) (Steinmetz, J., dissenting) (emphasis added).

201. Claussen v. Aetna Casualty & Sur. Co., 380 S.E.2d 686, 689-90 (Ga. 1989).

202. *Claussen*, 380 S.E.2d at 690 (emphasis added).

203. *See* 40 C.F.R. §§ 264.140-.151, 280.90-.116 (1995).

204. 18 SUPERFUND SITES, *supra* note 43, at 56.

create cleanup liability, but they also impose civil and criminal penalties—including fines *and imprisonment*—on parties who fail to follow detailed and complex regulations designed to prevent future pollution.[205] Since fines and penalties are intended to have a punitive effect and deter undesirable behavior, many jurisdictions hold them uninsurable as a matter of public policy,[206] and certainly no insurance policy operates as a get-out-of-jail-free card.

Further, a company's environmental practices have a significant impact on its corporate image because much information regarding its environmental performance is available to the public. For example, the above described fines and penalties are a matter of public record. Also, under federal and state community right-to-know laws, a company is required to disclose to the public and the government specific information on its spills and releases of toxic chemicals.[207] Additionally, federal securities laws and regulations also require detailed disclosure of a company's environmental liabilities for the benefit of investors.[208] With all this public disclosure, an industrial insured has an interest in assuring that it is perceived to be a good corporate citizen and not a polluter. A recent survey by Walker Research shows that the decisions of consumers, employees and investors are all influenced by a company's perceived record on social responsibility issues, including environmental matters.[209]

Finally, because of the breadth of CERCLA's liability scheme, an industrial insured has an interest in assuring that its real

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205. *See, e.g.*, 42 U.S.C. § 6928 (1988) (civil and criminal enforcement under the Solid Waste Disposal Act); 33 U.S.C. § 1319 (1994) (civil and criminal enforcement under the Clean Water Act); 42 U.S.C. § 7413 (1988 & Supp. V 1993) (civil and criminal enforcement under the Clean Air Act).

206. *See, e.g., In re* Texas E. Transmission Corp. PCB Contamination Ins. Coverage Litig., 870 F. Supp 1293, 1338-39 (E.D. Pa. 1992) (holding that penalties imposed by environmental agencies are not insurable under Pennsylvania and New Jersey law, but can be insurable under Texas law), *aff'd on other grounds*, 15 F.3d 1230 (3d Cir.), *cert denied sub nom.* Texas E. Transmission Corp. v. Fidelity & Casualty Ins. Co. of N.Y., 115 S. Ct. 291 (1994). *See* Michael A. Pope, *Punitive Damages: When, Where and How They are Covered*, 62 DEF. COUNS. J. 539 (1995).

207. *See, e.g.*, The Emergency Planning and Community Right-To-Know Act of 1986, 42 U.S.C. §§ 11001-11050 (1988 & Supp. V 1993). For a survey of the state community right-to-know laws, see DONALD W. STEVER & ELIZA A. DOLIN, 3 ENVIRONMENTAL LAW & PRACTICE ch. 6A (1995).

208. *See* Lisa J. Sotto, *Companies that Fail to Make Adequate Disclosure of Potential Environmental Liabilities under Superfund Have Become the Objects of Increased SEC Scrutiny*, NAT. L. J., Dec. 4, 1995, at B5 (citing 17 C.F.R. § 229.101, .103., .303 (information in registration statements) and *id.* § 240.10b-5 (1995) (antifraud provision)).

209. *See* WALKER RESEARCH, CORPORATE CHARACTER—IT'S DRIVING COMPETITIVE COMPANIES. WHERE'S IT DRIVING YOURS? (1994).

estate remains clean in order to protect its marketability. Today, environmental considerations affect every industrial real estate transaction, and pollution often adversely affects an owner's ability to mortgage, sell or lease property.[210]

2. *Public Policy Arguments in Favor of Coverage: Good Insurance Policy and Good Environmental Policy*

An accurate compass of current public policy on the pollution exclusion is the position taken by the states in their capacity as guardians of the public interest. This compass consistently points toward a pro-coverage interpretation. For example, state attorneys general who have submitted amicus briefs in pollution exclusion litigation have uniformly promoted the position of the policyholder—that the exclusion should be interpreted narrowly in favor of coverage.[211] Further, at least two state insurance commissioners have recently initiated regulatory reforms designed to protect policyholders with environmental claims.[212]

There are two important public policy goals promoted by a pro-coverage interpretation of the pollution exclusion—one makes for

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210. *See* Jeffrey M. Moss, Comment, *Impact of CERCLA on Real Estate Transactions: What Every Owner, Operator, Buyer, Lender, . . . Should Know*, 6 B.Y.U. J. PUB. L. 365 (1992).

211. *See* Dimmitt Chevrolet v. Southeastern Fidelity Ins. Corp., 636 So. 2d 700, 714 (Overton, J., dissenting from order denying rehearing) (citing amicus brief filed by the Attorney General of Florida); Morton Int'l, Inc. v. General Accident Ins. Co., 629 A.2d 831, 855 (N.J. 1993) (citing amicus briefs filed by the Attorneys General of New Jersey, Delaware, Pennsylvania, West Virginia and Indiana), *cert. denied*, 114 S. Ct. 2764 (1994). *See also* Salisbury, *supra* note 65, at 410-14 app. B (listing 26 amicus briefs filed by governmental entities in support of policyholders in environmental coverage litigation as of 1991).

212. Irene C. Warshauer et al., *States Initiate Environmental Insurance Reforms*, NAT'L L.J., Nov. 6, 1995, at C9. The Louisiana Insurance Commissioner is considering a proposal to abolish the use of the absolute pollution exclusion in that state, citing a study by his agency which "revealed that the 1970 and 1985 exclusions are 'being used [by the insurance industry] in a manner inconsistent with [their] intent and historical purposes.'" *Id.* (quoting Letter from C. Noel Wertz, Sr., Attorney to Louisiana Commissioner of Insurance James H. Brown, to Les Hammond, ISO (Aug. 12, 1994)) (second alteration in original).

In 1995, the Washington Insurance Commissioner adopted regulations governing the process by which environmental coverage claims are handled, designed to redirect resources from disputing such claims to cleaning up the environment. *See* WASH. ADMIN. CODE §§ 284-20-200, 284-30-900 to -940 (1995). The regulations, the first of their kind in the nation, were supported by small businesses, farmers and environmentalist groups, but opposed by the insurance industry. *See* Alex P. Fryer, *Pollution Insurance Rules Provoke Fierce Debate*, PUGET SOUND BUS. J., Feb. 17, 1995, at 9; Testimony of Deputy Insurance Commissioner George W. Taylor Before the Joint Administrative Rules Review Committee (Aug. 22, 1995).

See also infra note 214 (discussing New York's 1982 policy change towards the pollution exclusion).

good insurance policy and the other makes for good environmental policy.

First, a pro-coverage interpretation of the pollution exclusion based on the regulatory history of the clause would encourage candor on the part of the insurance industry when representing the intended effect of new policy language. Courts that refuse to entertain the compelling extrinsic evidence of the industry statements before state regulators are de facto rewarding the industry for their misrepresentations in 1970, thereby encouraging similar future conduct. The Attorney General of Florida feared just such an effect when he argued that:

> [T]he important public policy of protecting Florida consumers from misleading coverage representations would be reduced to a sham if insurers were permitted to characterize the pollution exclusion as a mere clarification in order to obtain regulatory approval and then characterize it in court papers as a radical reduction in coverage 23 years later at the point of claim. To protect the integrity of Florida's regulatory scheme, insurers . . . should be held to the formal explanations made to the Florida Insurance Department, which represents the interests of Florida citizens in approving and reviewing form endorsements.[213]

Second, a pro-coverage interpretation of the pollution exclusion clause is good environmental policy because it provides more resources for the daunting task ahead of cleanup, which is estimated to be in the hundreds of billions of dollars.[214] A pro-coverage interpretation will also serve to control transaction costs by redirecting insurers' resources from disputing environmental claims to indemnifying cleanup.[215]

The strict liability scheme of CERCLA is often criticized as flawed and unfair.[216] In theory, it purports to be a "polluter pays" system, but in practice, it is really a "deep pocket pays"

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213. *Dimmitt*, 636 So. 2d at 714 (Overton, J., dissenting from order denying rehearing) (quoting amicus brief filed by the Attorney General of Florida).

214. *See supra* notes 34-36 and accompanying text.

Indeed, the State of New York recognized the important role of insurance in environmental cleanup in 1982 when it reversed its earlier policy towards environmental insurance. Previously, in 1971, the New York State Legislature had passed a law making the pollution exclusion clause mandatory in all insurance policies. Hurwitz & Kohane, *supra* note 121, at 379 (citations omitted). The purpose of the law was to discourage intentional polluters. *Id.* However, the law was repealed in 1982, with a statement by then Governor Hugh Carey: "As we increasingly rely on the private sector to treat, store and dispose of hazardous wastes in a safe and environmentally sound manner, *we must insure that the public health is safeguarded from the adverse consequences of failures and accidents for which insufficient funds are available to remedy.*" *Id.* at 379-80 & n.6 (citations omitted) (emphasis added).

215. *See supra* notes 39-42 and accompanying text for a discussion of the excessive transaction costs involved in disputing environmental liability.

216. *See* Anderson, *supra* note 37.

system.[217] Superfund's definition of PRP fails to take into account the hard truth: We have seen the polluter and the polluter is us. "Us" includes the industrial firms which realized increased profits from inexpensive pre-1980 waste disposal practices, their suppliers who benefitted from a profitable and stable customer base, their employees whose livelihoods depended upon company viability, the consumer who benefitted from better and cheaper products, and yes, the insurers who collected premiums for CGL policies that were represented to provide coverage for unintentional pollution damage.

All of these parties must do their share. Industrial policyholders do their share through the CERCLA liability scheme. Individuals do their share through higher taxes and costs passed onto consumers through product pricing. The insurers must also do their share and should not be given a special dispensation from this important shared responsibility.

The insurance industry has demonstrated itself to be somewhat unwilling to meet this responsibility, not only in the litigious stance that it takes on environmental claims, but also in the position that it takes on congressional Superfund reform. The entire insurance industry advocates the repeal of retroactive liability prior to 1987.[218] Coincidentally, 1987 is the year after the insurance industry introduced the absolute pollution exclusion in the standard CGL policy.[219] In effect, under such a reform, the insurance industry's responsibility for Superfund cleanup is effectively eliminated—liability for pre-1987 occurrences is eliminated under the statutory repeal and liability for post-1987 occurrences is eliminated under the absolute pollution exclusion.

Although perhaps somewhat unwilling, current data shows that the insurance industry is not completely unprepared to meet this responsibility. In 1994, the A.M. Best Company had ex-

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217. The insurance industry also recognizes that Superfund liability is only "polluter pays" in theory and not in practice. *See Reform of Superfund Act of 1995: Hearings on H.R. 2500 Before the Subcomm. on Water Resources and Environment of the House Comm. on Transportation and Infrastructure*, 104th Cong., 1st Sess. (1995) (testimony of the American Insurance Association), *available in* Westlaw, 1995 WL 655210 (F.D.H.C.) [hereinafter AIA Testimony].

218. AIA Testimony, *supra* note 217.

219. This coincidence has not gone unnoticed by other stakeholders in the Superfund debate. *See Reform of Superfund Act of 1995: Hearings on H.R. 2500 Before the Subcomm. on Water Resources and Environment of the House Comm. on Transportation and Infrastructure*, 104th Cong., 1st Sess. (1995) (testimony of Karen Florini, Senior Attorney, Environmental Defense Fund), *available in* Westlaw, 1995 WL 655211 (F.D.C.H.); *Hearings Before the Subcomm. on Commerce, Trade and Hazardous Materials of the House Comm. on Commerce*, 104th Cong., 1st Sess. (1995) (testimony of Steven A. Herman, Assistant Administrator, Office of Enforcement and Compliance Assurance, EPA), *available in* Westlaw, 1995 WL 423251 (F.D.C.H.).

pressed concerns over the domestic insurance industry's ability to fund its ultimate environmental liabilities.[220] However, due to a combination of reduction in estimates of ultimate cleanup costs and an acceleration in industry reserve funding, A.M. Best now estimates that the domestic insurance industry has already reserved 38% of its ultimate environmental liabilities, and projects that it will be able to accrue the remainder of those reserves well in advance of ultimate payout.[221]

CONCLUSION

Billions of dollars in environmental coverage claims remain at stake in the jurisdictions that have yet to interpret the scope of the pollution exclusion. Courts that have yet to address the issue should reverse the trend of pro-insurer decisions of the last few years and interpret the clause in favor of coverage. The insurers' key to favorable decisions has been perpetuating the mechanical application of the plain meaning rule—long abrogated by modern contract scholars—to the exclusion of persuasive extrinsic evidence supporting a pro-coverage interpretation.

The insurance industry is large, well-organized, legislatively exempt from most antitrust laws and effective in promoting its interests. The courts, therefore, in applying well-recognized contract principles and rules of equity, must be effective in protecting the interests of policyholders. Such interests coincide with those of the public at large who benefit from the integrity of the insurance regulatory system, as well as from a cost-effective national environmental cleanup program.

Melody A. Hamel

220. BEST REPORT, *supra* note 36, at 1.
221. *Id.* at 4-5 & exhibit 2.